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# **STUDY MATERIAL**

## **EXECUTIVE PROGRAMME**

# **ECONOMIC AND COMMERCIAL LAWS**

## **PAPER 3**



**THE INSTITUTE OF  
Company Secretaries of India**

**IN PURSUIT OF PROFESSIONAL EXCELLENCE**

Statutory body under an Act of Parliament

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**EXECUTIVE PROGRAMME**  
**ECONOMIC AND COMMERCIAL LAWS**

India has made considerable economic progress since its Independence. Over the years, the various policy initiatives and economic reforms in India have made India one of the fastest growing economies in the world today. The emerging economic environment involving rapid technology changes, response in terms of change in methods, trade and services, globalisation of economy, liberalisation of trade and industry and emphasis on international competitiveness and bringing the existing laws in tune with the future market needs, the Government has also initiated legislative reforms in the area of economic and commercial laws. The Government enacted Foreign Exchange Management Act, The Competition Act, 2002 replacing the MRTP Act and amended the Consumer Protection Act in the year 2002. The Legal Metrology Act, 2009 replacing Standards of Weights and Measures Act, 1976 and Foreign Contribution (Regulation) Act, 2010 replacing Foreign Contribution (Regulation) Act, 1976. In the area of Intellectual property, the Government has enacted Trade Marks Act and Designs Act, and amended the Patents Act and the Copyright Act. In this regard the Government has further amended the Patents Act in 2005 and Copyright Act in 2012. The Foreign Trade Policy 2009-14 has also been announced in line with the reform agenda and amended from time to time. Further, the Prevention of Money Laundering Act to deal with new categories of economic offences, has also been made effective w.e.f. 1st July, 2005 and amended in 2009 and 2012. Similarly, in the area of Environment Laws, the process of reforms is going on and Parliament enacted National Green Tribunal Act, 2010.

In the light of above developments, this study material has been prepared to provide an understanding of certain economic and commercial legislations which have direct bearing on the functioning of companies. The study material has been divided into two parts consisting of fifteen study lessons. Part A consists of Study Lessons I to IX, whereas Part B consists of Study Lessons X to XV.

This study material has been published to aid the students in preparing for the Economic and Commercial Laws paper of the CS Executive Programme. It is part of the education kit and takes the students step by step through each phase of preparation stressing key concepts, pointers and procedures. Company Secretaryship being a professional course, the examination standards are set very high, with emphasis on knowledge of concepts, applications, procedures and case laws, for which sole reliance on the contents of this study material may not be enough. Besides, as per the Company Secretaries Regulations, 1982, students are expected to be conversant with the amendments to the laws made upto six months preceding the date of examination. The material may, therefore, be regarded as the basic material and must be read alongwith the original Bare Acts, Rules, Regulations, Case Law, as well as recommended readings given with each study lesson.

As the area of economic and commercial laws undergoes frequent changes, it becomes necessary for every student to constantly update himself with the various legislative changes made as well as judicial pronouncements rendered from time to time by referring to the Institute's journal 'Chartered Secretary' as well as other law/professional journals.

The legislative changes made upto June 30, 2014 have been incorporated in the study material. However, it may so happen that some developments might have taken place during the printing of the study material and its supply to the students. The students are therefore, advised to refer to the e-bulletin and other publications for updation of the study material.

In the event of any doubt, students may write to the Directorate of Academics in the Institute for clarification at [academics@icsi.edu](mailto:academics@icsi.edu). Although due care has been taken in publishing this study material yet the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

Should there be any discrepancy, error or omission noted in the study material, the Institute shall be obliged if the same are brought to its notice for issue of corrigendum in the 'e-bulletin'.

**EXECUTIVE PROGRAMME****SYLLABUS  
FOR****PAPER 3: ECONOMIC AND COMMERCIAL LAWS (100 Marks)**

**Level of Knowledge:**      **Part A**-Advance Knowledge  
**Part B**- Working Knowledge

**Objective:** *To acquire knowledge and understanding of Economic and Commercial Laws.*

**Detail Contents:****PART A: (70 Marks)****1. Foreign Exchange Management**

- Objectives and Definitions under FEMA, 1999
- Current Account Transactions and Capital Account Transactions
- FDI Policy
- Foreign Direct Investment in India and Abroad
- Acquisition and Transfer of Immovable Property in India and Abroad
- Establishment of Branch, Office etc. in India
- Export of Goods and Services
- Realization and Repatriation of Foreign Exchange
- Authorized Person
- Penalties and Enforcement
- Foreign Contribution ( Regulation )Act, 2010
- Foreign Contributions and Hospitality
- Exemptions
- Powers of Central Government
- Adjudication, Appeal and Compounding
- Offences and Penalties

**2. Foreign Trade Policy and Procedures**

- Main Features
- Special Focus Initiatives
- Served from India Scheme
- Export Promotion Council
- Vishesh Krishi and Gram Udyog Yojana

- Focus Market Scheme; Focus Product Scheme; Duty Exemption and Remission Schemes; Advance Authorization Scheme; DFRC; DEPB; EPCG, etc.
- EOUs, EHTPs, STPs, BPTs and SEZs

### **3. Competition and Consumer Protection**

- Concept of Competition
- Development of Competition Law
- Competition Policy
- Competition Act, 2002 – Anti Competitive Agreements, Abuse of Dominant Position, Combination, Regulation of Combinations, Competition Commission of India; Appearance before Commission, Compliance of Competition Law
- Consumer Protection Act, 1986
- Consumer Protection in India
- Genesis of the Law and Objects
- Rights of Consumers
- Nature and Scope of Remedies
- Appearance before Consumer Dispute Redressal Forums

### **4. Intellectual Property Rights**

- Introduction – GATT, WIPO and TRIPS
- Concept and Development of Intellectual Property Law in India
- Law and Procedure Relating to Patents, Trade Marks and Copyrights
- Geographical Indications
- Design Act
- Overview of Laws Relating to Other Intellectual Property Rights
- Intellectual Property Appellate Board

### **5. Law relating to Arbitration and Conciliation**

- Introduction to UNCITRAL MODEL LAW
- Law of Arbitration in India
- Types of Arbitration
- Appointment of Arbitrators – Procedure
- Judicial Intervention
- Venue – Commencement
- Award – Time limit, Enforceability, Interest
- Recourse against Award – Appeals
- Conciliation and Compromise
- International Commercial Arbitration ; Foreign Awards
- Arbitration Agencies – ICADR, ICA, Chambers of Commerce, Professional Arbitrators
- Alternate Disputes Resolution

### **6. Law relating to Transfer of Property**

- Important Definitions
- Types of Properties

- Movable and Immovable Property
- Properties which cannot be Transferred
- Rule Against Perpetuities
- Lis Pendens
- Provisions Relating to Sale
- Mortgage, Charge, Lease, Gift and Actionable Claim

#### **7. Law relating to Stamps**

- Methods of Stamping
- Consequences of Non-Stamping and Under-Stamping
- Impounding of Instruments
- Construction of Instruments for Determination of Stamp Duty Payable
- Adjudication
- Allowance and Refund
- Penal Provisions
- Concept of E-Stamping

#### **8. Law relating to Contract**

- Contract – Introduction
- Legality of Objects
- Standard Form of Contract
- Multinational Agreement
- E-Contracts
- Strategies and Constraints to enforce Contractual Obligations
- Special Contracts: Indemnity and Guarantee; Bailment and Pledge; Law of Agency

#### **9. Prevention of Money Laundering**

- Genesis
- Prevention of Money Laundering Act, 2005
- Concept and Definitions, Various Transactions, etc.
- Obligations of Banks and Financial Institutions
- RBI Guidelines on KYC

### **PART B: (30 Marks)**

#### **10. Law relating to Essential Commodities, Weights and Measures**

- Overview of Essential Commodities Act, 1955
- Objects
- Powers of Central Government
- Seizure and Confiscation of Essential Commodities
- Summary Trial
- The Legal Metrology Act, 2009

#### **11. Law relating to Societies**

- General Concept Relating to Registration of Societies
- Property of Societies

- Suits by and against Societies
- Enforcement of Judgment against Societies
- Dissolution of Societies

## **12. Law relating to Trusts**

- General Concept relating to Trusts
- Creation of Trust
- Duties and Liabilities of Trustees
- Rights and Powers of Trustees, Disabilities of Trustees
- Rights and Liabilities of the Beneficiary

## **13. Industries Development and Regulation**

- Objects and Definitions
- An Overview of Industrial Policy
- Regulatory Mechanism under IDRA
- The Micro, Small and Medium Enterprises Development Act, 2006

## **14. Law relating to Pollution Control and Environmental Protection**

- Concept of Sustainable Development and Bio Diversity
- Government Policy Regarding Environment
- Law Relating to Prevention and Control of Air Pollution and Water pollution
- Environment (Protection) Act, 1986
- National Green Tribunal
- Appearance before Environment Tribunal/Authority
- Public Liability Insurance Act, 1991

## **15. Law relating to Registration of Documents**

- Registration of Documents – Compulsory and Optional
- Time and Place of Registration
- Consequences of Non-Registration
- Description of Property
- Miscellaneous Provisions

**LIST OF RECOMMENDED BOOKS**  
**ECONOMIC AND LABOUR LAWS**

**Recommended Readings and References:**

1. Vinod Dhall : Competition Law Today – Concepts, Issues and the Law in Practice; Oxford University Press, New Delhi.
2. T. Ramappa : Competition Law in India – Policies, Issues, and Developments; Oxford University Press, New Delhi.
3. ICSI : Practitioner's Guide to Consumer Protection Law.
4. Dr. K.R. Chandratre : Handbook on Consumer Protection Law; Vidhi Publishing, New Delhi.
5. Dr. V.K. Aggarwal : Consumer Protection Law and Practice; Bharat Law House, 22, Tarun Enclave, Pitampura, New Delhi - 110 034.
6. Dr. Gurbax Singh : Law of Consumer Protection; Bharat Law Publications, 22, Tarun Enclave, Pitampura, New Delhi - 110 034.
7. Kuldeep Saxena : Consumer Protection Act & Rules, Law Links.
8. Sumeet Malik : Environmental Law; Eastern Book Company, Lucknow.
9. Dr. H.N. Tripathi : The Environment Pollution Control Manual; Hari Law Agency, Allahabad.
10. Lall's : Commentaries on Water and Air Pollution Laws; Delhi Law House, Delhi.
11. Rajiv Jain : Guide to New Industrial Policy, with Procedure; India Investment Publications, New Delhi.
12. Bare Act : Prevention of Money-Laundering Act.
13. Richard Parlour : International Guide to Money-Laundering Law and Practice.
14. Bare Act : Foreign Exchange Management Act.
15. SnowWhite : Foreign Exchange Management Manual.
16. S.K. Roy Chaudhary & H.K. Saharay : The Law of Trademarks, Copyright, Patents and Design.
17. B.L. Wadehra : Law Relating to Patents, Trademarks, Copyright, Designs and Geographical Indications.
18. Aswani Kr. Bansal : Law of Trademarks in India.
19. Satyawrat Ponkse : The Management of Intellectual Property.

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|-----|-----------------------------------|---|--|
| 20. | Ministry of Commerce & Industry   | : | Foreign Trade Policy and Procedure.  |
| 21. | A.M. Satarvad                     | : | Mulla on the Transfer of Property Act, 1882; N.M. Tripathy Pvt. Ltd., Bombay |
| 22. | S.K. Roy Chowdhary & H.K. Saharay | : | Law of Arbitration and Conciliation; Eastern Law House, Calcutta             |

**Note:**

- (i) Students are advised to read the relevant Bare Acts.
- (ii) The latest available editions of the books referred to above may be read.
- (iii) Students may refer e-bulletin available on ICSI website [www.icsi.edu](http://www.icsi.edu) regularly for academic guidance.

**ARRANGEMENT OF STUDY LESSONS**

<i>Lesson No.</i>	<i>Subject</i>
<b>PAPER 3: ECONOMIC AND COMMERCIAL LAWS (100 Marks)</b>	

**PART A**

- I. Foreign Exchange Management
- II. Foreign Trade Policy and Procedures
- III. Competition and Consumer Protection
- IV. Intellectual Property Rights
- V. Law relating to Arbitration and Conciliation
- VI. Law relating to Transfer of Property
- VII. Law relating to Stamps
- VIII. Law relating to Contract
- IX. Prevention of Money Laundering

**PART B**

- X. Law relating to Essential Commodities, Weights and Measures
- XI. Law relating to Societies
- XII. Law relating to Trusts
- XIII. Industries Development and Regulation
- XIV. Law relating to Pollution Control and Environmental Protection
- XV. Law relating to Registration of Documents

**TEST PAPERS**

EXECUTIVE PROGRAMME  
ECONOMIC AND COMMERCIAL LAWS

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# Lesson 1

## FOREIGN EXCHANGE MANAGEMENT

### Section I

#### LESSON OUTLINE

- Objective of FEMA, 1999
- Foreign Exchange
- Foreign Securities
- FDI Policy
- Current Account Transactions
- Capital Account Transactions
- Foreign Direct Investment in India
- Direct Investment outside India
- Acquisition & Transfer of immovable property in India.
- Acquisition & Transfer of immovable property outside India.
- Establishment of Branch office in India
- Export of Goods and services
- Realisation & Repatriation of foreign exchange
- Authorised Person
- Compounding of offences
- Penalties and Enforcement
- Adjudication and Appeal
- Appointment of Adjudicating Authority
- Appeal to Special Director
- Establishment of Appellate Tribunal
- Appeal to High Court
- Directorate of Enforcement

#### LEARNING OBJECTIVES

As per Article 246 of the Constitution of India, the Parliament has exclusive power to make laws with respect to any of the matters enumerated in the Union List in the Seventh Schedule. The Foreign Exchange Management Act, 1999 can be traced to various entries in the Union List. Entry 16 of the Union List deals with Foreign jurisdiction. Entry 36 of the Union List deals with Currency, coinage and legal tender; foreign exchange. Entry 37 of the Union List deals with Foreign loans and Entry 41 of the Union List deals with Trade and commerce with foreign countries; import and export across customs frontiers; definition of customs frontiers.

When a business enterprise imports goods from other countries, exports its products to them or makes investments abroad, it deals in foreign exchange. Foreign exchange means 'foreign currency' and includes deposits, credits and balances payable in any foreign currency; drafts, travellers' cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency; and drafts, travellers' cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency.

The management of foreign exchange is very important in the present day business. This lesson deals with how FEMA facilitates external trade and payments and promotes the orderly development and maintenance of foreign exchange market. The Act has assigned an important role to the Reserve Bank of India (RBI) in the administration of FEMA. The rules, regulations and norms pertaining to several sections of the Act are laid down by the Reserve Bank of India, in consultation with the Central Government.

Foreign Exchange Management Act, 1999 is an Act to facilitate external trade and payments and for promoting the orderly development and maintenance of foreign exchange market in India.

## INTRODUCTION

The Foreign Exchange Regulation Act, 1973, which was enacted to consolidate and amend the law in several respects encompassing the experience gained over few decades of implementation of the earlier enactment of 1947, outlived its purpose in the light of the liberalization policies introduced in 1991.

The Foreign Exchange Regulation Act, since then had been reviewed and amendments were made as part of the on going process of economic liberalization relating to foreign investment and foreign trade for closer interaction with the world economy. During the subsequent period, the Central Government decided further review of the Foreign Exchange Regulation Act in the light of developments and experience in relation to foreign trade and investment. It was at that time felt, that a better course would be to repeal the Foreign Exchange Regulation Act and enact a new legislation.

Taking into consideration the developments such as substantial increase in foreign exchanges reserves, growth in foreign trade, rationalization of tariffs, current account convertibility etc., the Foreign Exchange Management Bill, to repeal and replace the Foreign Exchange Regulation Act was introduced in the Lok Sabha. But before the Bill came up for discussion and approval, the Lok Sabha was dissolved. Subsequently, certain modifications were made to the original Bill and a modified Bill was presented and passed by both the Houses of Parliament. The Foreign Exchange Management Act received the assent of the President on 9th December, 1999 and brought into force with effect from 1.6.2000.

## DEFINITIONS

Section 2 of the Foreign Exchange Management Act defines various terms used in the Act, as given below:

### ***Adjudicating Authority [Section 2(a)]***

According to clause (a) of Section 2 'Adjudicating Authority' means an officer authorised under Sub-section (1) of Section 16 for the purposes of adjudication in respect of penalties under Section 13. Section 16 empowers the Central Government, to appoint, by an order published in the Official Gazette, as many officers as it may think fit as the adjudicating authorities for holding an enquiry in the manner prescribed after giving the person alleged to have committed any contravention, an opportunity of being heard.

### ***Appellate Tribunal [Section 2(b)]***

'Appellate Tribunal' means Appellate Tribunal for Foreign Exchange to hear appeals against the orders of the adjudicating authorities and Special Directors (Appeals) under the Act.

### ***Authorised Person [Section 2(c)]***

The term authorised person is defined to include an authorised dealer, money changer, offshore banking unit or any other person for the time being authorised to deal in foreign exchange or foreign securities.

### ***Capital Account Transaction [Section 2(e)]***

'Capital account transaction' has been defined to mean any transaction which alters the assets or liabilities including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of person resident outside India and includes the transactions specified in Sub-section (3) of Section 6 of the Act.

***Currency Notes [Section 2(i)]***

'Currency Notes' means and includes cash in the form of coins and bank notes. In fact, it means money and such bank notes or other paper money as are authorised by law and circulate from hand to hand as a medium of exchange.

***Current Account Transaction [Section 2(j)]***

The term current account transaction has been defined to mean a transaction other than a capital account transaction and includes payments due in connection with foreign trade, other current business, services and short term banking and credit facilities in the ordinary course of business; payments due as interest on loan and as net income from investments; remittances for living expenses of parents, spouse and children residing abroad and expenses in connection with foreign travel, education and medical care of parents, spouse and children.

Under the Act freedom has been granted for selling and drawing of foreign exchange to or from an authorized person for undertaking current account transactions. However, the Central Government has been vested with powers in consultation with Reserve Bank to impose reasonable restrictions on current account transactions. The Central Government has framed Foreign Exchange Management (Current Account Transactions) Rules, 2000 dealing with various aspects of current account transactions.

***Foreign Exchange [Section 2(n)]***

The term 'foreign exchange has been defined to mean foreign currency and includes deposits, credits, balance payable in foreign currency, drafts, travellers cheques, letters of credit, bills of exchange expressed or drawn in Indian currency but payable in any foreign currency. Any draft, travellers cheque, letters of credit or bills of exchange drawn by banks, institutions or persons outside India but payable in Indian currency has also been included in the definition of foreign exchange.

***Foreign Security [Section 2(o)]***

The term Foreign Security has been defined to mean any security, in the form of shares, stocks, bonds, debentures or any other instrument denominated or expressed in foreign currency and includes securities expressed in foreign currency but where redemption or any form of return such as interest or dividend is payable in Indian currency.

Transfer or issue of a foreign security is a capital account transaction within the meaning of Section 6(3)(a) of the Act. The Reserve Bank of India has made Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2000 for regulation, acquisition and transfer of a foreign security by a person resident in India i.e. investment by Indian entities in overseas joint ventures and wholly owned subsidiaries as also investment by a person resident in India in shares and securities issued outside India.

***Person [Section 2(u)]***

The definition of the term 'person includes, an individual, a Hindu Undivided Family, a company, a firm, an association of persons or body of individuals whether incorporated or not; any agency, office or branch owned or controlled by such persons. Even every artificial juridical person not falling within the above definition has been treated as person as per clause (u) of Section 2.

***Person Resident in India [Section 2(v)]***

The expression 'Person resident in India has been defined to mean a person residing in India for more than 182 days during the course of the preceding financial year. However, two categories of persons are excluded from the purview of definition.

## 4 EP-ECL

The first category includes any person who has gone out of India or who stays outside India for or on taking up employment outside India, or for carrying on outside India a business or vocation. The definition also includes person who stays outside India for any other purpose in such circumstances as would indicate his intention to stay outside India for an uncertain period. The second category of persons which have been excluded from the definition of person resident in India include:

A person who has come to stay or stays in India, in either case otherwise than—

- (i) for or taking up employment in India; or
- (ii) for carrying on in India a business or vocation in India; or
- (iii) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period.

## REGULATION AND MANAGEMENT OF FOREIGN EXCHANGE

Chapter II of the Act containing Sections 3-9 deals with Regulation and Management of Foreign Exchange. Section 3 prohibits any person other than an authorised person from dealing in or transferring any foreign exchange or foreign security to any person or making any payment to or for the credit of any person resident outside India in any manner or receiving otherwise through an authorised person any payment by order or on behalf of any person resident outside India in any manner except as provided in the Act, rules or regulations made thereunder or with the general or special permission of the Reserve Bank of India.

Section 3(d) prohibits a person to enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person, except as otherwise provided in the Act and rules or regulations made thereunder. For this purpose, financial transaction has been defined to mean making any payment to or for the credit of any person or receiving any payment for, by order or on behalf of any person. Financial transaction also include drawing, issuing or negotiating any bill of exchange or promissory note or transferring any security or acknowledging any debt.

## CURRENT ACCOUNT TRANSACTIONS

Section 5 of the Act allows any person to sell or draw foreign exchange to or from an authorised person if such sale or drawal is a current account transaction as defined under Section 2(j) of the Act. However, the Central Government may, in the public interest and in consultation with the Reserve Bank impose reasonable restrictions for current account transactions.

Foreign Exchange Management (Current Account Transactions) Rules, 2000 defines the term 'Drawal' as to mean drawal of foreign exchange from an authorised person and includes opening of Letter of Credit or use of International Credit Card or International Debit Card or ATM Card or any other thing by whatever name called which has the effect of creating foreign exchange liability.

## Prohibition on drawal of foreign exchange for certain transactions

Rule 3 prohibits the drawal of foreign exchange for the purposes of transactions specified in the Schedule I or a travel to Nepal and/or Bhutan or a transaction with a person resident in Nepal or Bhutan. However, in the case of transaction with a person resident in Nepal and Bhutan, the prohibition may be exempted by RBI subject to such terms and conditions as it may consider necessary. Schedule I to the Rules enumerate the situations in which the drawal of foreign exchange is prohibited. These are as follows:

- (a) Remittance out of lottery winnings;

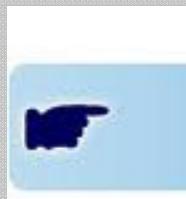
- (b) Remittance of income from racing/riding etc. or any other hobby;
- (c) Remittance for purchase of lottery tickets, banned/prescribed magazine, football pools, sweep stakes etc.
- (d) Payment of commission on exports made towards equity investment in joint ventures/wholly owned subsidiaries abroad of Indian Companies.
- (e) Payment of Commission on exports under Rupee State Credit Route, except commission upto 10% of invoice value of exports of tea and tobacco.
- (f) Payment related to 'call back service' of telephone.
- (g) Remittance of interest income on funds held in Non-resident Special Rupee Scheme Account.

### **Prior approval of Government of India for certain transactions**

Rule 4 requires prior approval of the Government of India for the transactions as specified in Schedule II. However, this does not apply to the cases where the payment is made out of funds held in Resident Foreign Currency Account (RFC) of the remitter.

#### **Illustration**

***Mr. Y, a person resident in India, desires to take a life insurance policy from a foreign insurance company, the yearly premium of which is US\$ 25, 000.***



*"Mr. Y, a person resident in India, can take a life insurance policy from a foreign insurance company with a yearly premium of US\$25,000(VIDE-A.P.(DIR SERIES) CIRCULAR NO. 76, DATED 24/02/2004 ISSUED BY RBI). Earlier, as per Rule 4 read with Schedule II to the Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000, payment for securing insurance for health from a company abroad required prior permission of Central Government".*

### **Prior approval of RBI for certain transactions**

Rule 5 requires prior approval of the Reserve Bank in the following cases:

1. Release of exchange exceeding US\$ 10,000 or its equivalent in one calendar year, for one or more private visits to any country (except Nepal and Bhutan).
2. Gift remittances exceeding US\$ 5,000 per remitter/donor per annum.
3. Donation exceeding US\$ 5,000 per remitter/donor per annum.
4. Exchange facilities exceeding US\$ 1, 00,000 for persons going abroad for employment.
5. Exchange facilities exceeding US\$ 1, 00,000 for emigration or exceeding the amount prescribed by country of emigration.
6. Remittance for maintenance of close relatives abroad—
  - (i) exceeding net salary (after deduction of taxes, contribution to provident fund and other deductions) of a person who is resident but not permanently resident in India and:
    - (a) is a citizen of a foreign state other than Pakistan;
    - (b) is a citizen of India, who is on deputation to the office or branch or subsidiary or a joint venture in India of such foreign company.

- (ii) exceeding US\$ 100,000 per year per recipient, in all other cases.

It has been explained that the item, “a person resident in India on account of his employment or deputation of a specified duration (irrespective of length thereof) or a specific job or assignment the duration of which does not exceed three years, is a resident but not permanently resident.”

7. Release of foreign exchange, exceeding US\$ 25,000 to a person, irrespective of period of stay, for business travel, or attending a conference or specialised training or maintenance expenses of a patient going abroad for medical treatment or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/check-up.
8. Release of foreign exchange for meeting expenses for medical treatment exceeding US\$ 100,000 or its equivalent.
9. Release of exchange for studies abroad exceeding the estimates from the institution abroad or US\$ 1, 00,000 per academic year whichever is higher.
10. Commission per transaction to agents abroad for sale of residential flats/commercial plots in India exceeding the limits of US\$ 25,000 or 5 per cent of the inward remittance, per transaction, whichever is higher.
11. Remittances exceeding US\$ 1 million per project for any consultancy services procured from abroad.
13. Remittance exceeding US\$ 1, 00,000 by an entity in India by way of reimbursement of pre-incorporation expenses.

However, this Rule shall not apply where the payment is made out of funds held in Resident Foreign Currency (RFC) Account of the remitter.

Rule 7 provides that in case of use of International Credit Card for making payment by a person towards meeting expenses while such person is on visit outside India the prior approval of Reserve Bank shall not be required for transactions included in Schedule III.

Vide a circular dated 14th June, 2005, it has been clarified that International Debit Cards can also be used by a resident for drawing cash or making payment to a merchant establishment overseas during his visit abroad for permissible current account transactions and itemwise limits as mentioned in the schedules shall be applicable to payment made through use of these cards.

#### ***How much foreign exchange is available to a person going abroad on emigration?***



A person going abroad on emigration can draw foreign exchange from AD Category I bank and AD Category II up to the amount prescribed by the country of emigration or USD 100,000. He can draw foreign exchange up to USD 100,000 on self-declaration basis from an Authorised Dealer in India. This amount is only to meet the incidental expenses in the country of emigration. No amount of foreign exchange can be remitted outside India to become eligible or for earning points or credits for immigration. All such remittances require prior permission of the Reserve Bank. If requirement exceeds USD 100,000, the person requires to obtain the prior approval from the Reserve Bank.

#### **CAPITAL ACCOUNT TRANSACTION**

Section 6 allows capital account transactions subject however to certain conditions. This section empowers the Reserve Bank of India to specify, in consultation with the Central Government, any class or classes of capital account transactions permissible and the limit upto which foreign exchange shall be admissible for

such transactions. However, Reserve Bank shall not impose any restrictions on the drawal of foreign exchange for payments due on account of amortization of loans or for depreciation of direct investments in the ordinary course of business.

The Reserve Bank of India may, by regulations, prohibit, restrict or regulate the transfer or issue of any foreign security by a person resident in India or by a person resident outside India. Reserve Bank of India may also regulate, prohibit or restrict transfer or issue of any security or foreign security through any branch office, or agency in India of a person resident outside India. Any borrowing or lending in foreign exchange in whatever form or by whatever name called may also be regulated or prohibited by the Reserve Bank. Similarly, RBI may also prohibit or restrict any borrowing or lending in rupees in whatever form or by whatever name called between a person resident in India and a person resident outside India. Deposits between persons resident in India and persons resident outside India may be regulated or prohibited by the Reserve Bank of India. RBI may also regulate the export, import or holding of currency or currency notes.

Acquisition or transfer of immovable property other than on lease not exceeding five years in India by person resident in India or a person resident outside India may be prohibited or regulated by the Reserve Bank of India. RBI has also been empowered to prohibit or regulate giving of guarantee or surety in respect of any debt, obligation or other liability incurred by a person resident in India and owed to a person resident outside India or by a person resident outside India.

Sub-section (4) allows a person resident in India to hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India, if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India. Similarly, a person resident outside India is permitted to hold, own, transfer or invest in Indian currency, security, or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India.

Reserve Bank of India under Sub-section (6) has been empowered to regulate, prohibit, restrict establishment in India of a branch, office or other place of business by a person resident outside India for carrying on any activity relating to such branch, office or other place of business.

### **Permissible Capital Account Transactions**

Schedule I & II to Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000 classifies the capital account transactions of a person under the following two heads viz.

1. Classes of capital account transactions of persons resident in India.
2. Classes of capital account transactions of persons resident outside India.

### ***Classes of Capital Account Transactions of Persons Resident in India***

- (i) investment by a person resident in India in foreign securities.
- (ii) foreign currency loans raised in India and abroad by a person resident in India;
- (iii) transfer of immovable property outside India by a person resident in India;
- (iv) guarantees issued by a person resident in India in favour of a person resident outside India;
- (v) export, import and holding of currency/currency notes;
- (vi) loans and overdrafts by a person resident in India from a person resident outside India;
- (vii) maintenance of foreign currency accounts in India and outside India by a person resident in India;

- (viii) taking out of insurance policy by a person resident in India from an insurance company outside India;
- (ix) loans and overdrafts by a person resident in India to a person resident outside India;
- (x) remittance outside India of capital assets of a person resident in India;
- (xi) sale and purchase of foreign exchange derivatives in India and abroad and commodity derivatives abroad by a person resident in India.

However, Notification No. FEMA.165 /2007-RB Dated October 10, 2007 on Foreign Exchange Management (Permissible Capital Account Transactions) (Amendment) Regulations, 2007 provides that subject to the provisions of the Act or the rules or regulations or directions or orders made or issued thereunder, a resident individual may, draw from an authorized person foreign exchange not exceeding USD 50,000 per financial year with effect from December 20, 2006, USD 100,000 per financial year with effect from May 8, 2007 and USD 2,00,000 per financial year with effect from September 26, 2007, for a capital account transaction specified in Schedule I.

It may be noted that no part of the foreign exchange of USD 50,000 or USD 100,000 or USD 200,000, as the case may be, drawn can be used for remittance directly or indirectly to countries notified as non-co-operative countries and territories by Financial Action Task Force (FATF) from time to time and communicated by the Reserve Bank of India to all concerned."

#### ***Classes of Capital Account Transactions of Persons Resident Outside India***

- (i) Investment in India by a person resident outside India, that is to say:
  - (a) issue of security by a body corporate or an entity in India and investment therein by a person resident outside India; and
  - (b) investment by way of contribution by a person resident outside India to the capital of a firm or a proprietorship concern or an association of persons in India.
- (ii) Acquisition and transfer of immovable property in India by a person resident outside India.
- (iii) Guarantee by a person resident outside India in favour of, or on behalf of a person resident in India.
- (iv) Import and export of currency/currency notes into/from India by a person resident outside India.
- (v) Deposits between a person resident in India and a person resident outside India.
- (vi) Foreign Currency accounts in India of a person resident outside India.
- (vii) Remittance outside India of capital assets in India of a person resident outside India.

Subject to the provisions of the Act, or the rules, or regulations or directions or orders made or issued thereunder, any person may sell or draw foreign exchange to or from an authorised person for the above mentioned capital account transactions provided the transactions are within the limit, if any, specified in the Regulations relevant to the transaction. However, no person is allowed to undertake or sell or draw foreign exchange to or from an authorised person for any capital account transaction except as provided in the Act, Rules or regulations made thereunder.

Similarly, except as otherwise provided in the Act, no person resident outside India is entitled to make investment in India, in any form, in any company or partnership firm or proprietary concern or any entity whether incorporated or not, which is engaged or proposed to engage in the business of chit funds, or Nidhi company, or in agricultural or plantation activities, or real estate business, or construction of farm houses, or trading in Transferable Development Rights (TDRs). For this purpose real estate business includes development of townships, construction of residential/commercial premises, roads or bridges.

The payment for investment are required to be made by remittance from abroad through normal banking channels or by debit to an account of the investor maintained with an authorised person in India in accordance with the regulation made by the Reserve Bank of India. Every person selling or drawing foreign exchange to or from an authorised person for a capital account transaction is required to furnish to Reserve Bank a declaration within the time specified in the regulations relevant to the transactions.

## FOREIGN DIRECT INVESTMENTS IN INDIA

### INTRODUCTION

Foreign Direct Investment (FDI) is a category of cross border investment made by a resident in one economy (the direct investor) with the objective of establishing a 'lasting interest' in an enterprise (the direct investment enterprise) i.e. resident in an economy other than that of the direct investor. The motivation of the direct investor is a strategic long term relationship with the direct investment enterprise to ensure the significant degree of influence by the direct investor in the management of the direct investment enterprise. The objectives of direct investment are different from those of portfolio investment whereby investors do not generally expect to influence the management of the enterprise.

Foreign Direct Investment (FDI) in India is undertaken in accordance with the FDI Policy which is formulated and announced by the Government of India. The Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India issues a "Consolidated FDI Policy" on an yearly basis on March 31 of each year (since 2010) elaborating the policy and the process in respect of FDI in India. The latest Consolidated FDI Policy governed by the provisions of the Foreign Exchange Management Act (FEMA), 1999. FEMA Regulations which prescribe amongst other things the mode of investments i.e. issue or acquisition of shares / convertible debentures and preference shares, manner of receipt of funds, pricing guidelines and reporting of the investments to the Reserve Bank

### DEFINITIONS OF FDI POLICY

**'AD Category-I Bank'** means a bank (Scheduled Commercial, State or Urban Cooperative) which are authorized under Section 10(1) of FEMA to undertake all current and capital account transactions according to the directions issued by the RBI from time to time.

**'Authorized Bank'** means a bank including a co-operative bank (other than an authorized dealer) authorized by the Reserve Bank to maintain an account of a person resident outside India

**'Authorized Dealer'** means a person authorized as an authorized dealer under subsection (1) of section 10 of FEMA.

**'Authorized Person'** means an authorized dealer, money changer, offshore banking unit or any other person for the time being authorized under Sub-section (a) of Section 10 of FEMA to deal in foreign exchange or foreign securities.

**'Capital'** means equity shares; fully, compulsorily & mandatorily convertible preference shares; fully, compulsorily & mandatorily convertible debentures.

Note: Any other type of instruments like warrants, partly paid shares etc. are not considered as capital and cannot be issued to person resident outside India.

**'Capital account transaction'** means a transaction which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of persons resident outside India, and includes transactions referred to in sub-section (3) of section 6 of FEMA.

A company is considered as “**Controlled**” by resident Indian citizens if the resident Indian citizens and Indian companies, which are owned and controlled by resident, Indian citizens, have the power to appoint a majority of its directors in that company.

An entity is considered as ‘Controlled’ by ‘non resident entities’, if non-residents have the power to appoint a majority of its directors.

‘**Depository Receipt**’ (DR) means a negotiable security issued outside India by a Depository bank, on behalf of an Indian company, which represent the local Rupee denominated equity shares of the company held as deposit by a Custodian bank in India. DRs are traded on Stock Exchanges in the US, Singapore, Luxembourg, etc. DRs listed and traded in the US markets are known as American Depository Receipts (ADRs) and those listed and traded anywhere/elsewhere are known as Global Depository Receipts (GDRs).

‘**Erstwhile Overseas Corporate Body**’ (OCB) means a company, partnership firm, society and other corporate body owned directly or indirectly to the extent of at least sixty percent by non-resident Indian and includes overseas trust in which not less than sixty percent beneficial interest is held by non-resident Indian directly or indirectly but irrevocably and which was in existence on the date of commencement of the Foreign Exchange Management (Withdrawal of General Permission to Overseas Corporate Bodies (OCBs) ) Regulations, 2003 (the Regulations) and immediately prior to such commencement was eligible to undertake transactions pursuant to the general permission granted under the Regulations.

‘**Foreign Currency Convertible Bonds**’ (FCCB) means a bond issued by an Indian company expressed in foreign currency, the principal and interest of which is payable in foreign currency. FCCBs are issued in accordance with the Foreign Currency Convertible Bonds and ordinary shares (through depository receipt mechanism) Scheme 1993 and subscribed by a non-resident entity in foreign currency and convertible into ordinary shares of the issuing company in any manner, either in whole, or in part.

‘**FDI**’ means investment by non-resident entity/person resident outside India in the capital of the Indian company under Schedule 1 of FEM (Transfer or Issue of Security by a Person Resident outside India) Regulations 2000.

‘**FEMA**’ means the Foreign Exchange Management Act 1999 (42 of 1999).

‘**FIPB**’ means the Foreign Investment Promotion Board constituted by the Government of India.

‘**Foreign Institutional Investor**’ (FII) means an entity established or incorporated outside India which proposes to make investment in India and which is registered as a FII in accordance with the SEBI (FII) Regulations 1995.

‘**Foreign Venture Capital Investor**’ (FVCI) means an investor incorporated and established outside India, which is registered under the Securities and Exchange Board of India (Foreign Venture Capital Investor) Regulations, 2000 {SEBI(FVCI) Regulations} and proposes to make investment in accordance with these Regulations.

‘**Government route**’ means that investment in the capital of resident entities by nonresident entities can be made only with the prior approval from FIPB, Ministry of Finance or SIA, DIPP as the case may be.

‘**Holding Company**’ would have the same meaning as defined in Companies Act 1956.

‘**Indian Company**’ means a company incorporated in India under the Companies Act, 1956.

‘**Indian Venture Capital Undertaking**’ (IVCU) means an Indian company:

- (i) whose shares are not listed in a recognised stock exchange in India;

(ii) which is engaged in the business of providing services, production or manufacture of articles or things, but does not include such activities or sectors which are specified in the negative list by the SEBI, with approval of Central Government, by notification in the Official Gazette in this behalf.

**'Investing Company'** means an Indian Company holding only investments in another Indian company, directly or indirectly, other than for trading of such holdings/securities.

**'Investment on repatriable basis'** means investment, the sale proceeds of which, net of taxes, are eligible to be repatriated out of India and the expression 'investment on non-repatriable basis' shall be construed accordingly.

**'Joint Venture' (JV)** means an Indian entity incorporated in accordance with the laws and regulations in India in whose capital a foreign entity makes an investment.

**'Non resident entity'** means a 'person resident outside India' as defined under FEMA

**'Non Resident Indian' (NRI)** means an individual resident outside India who is a citizen of India or is an individual of Indian origin.

A company is considered as '**Owned**' by resident Indian citizens if more than 50% of the capital in it is beneficially owned by resident Indian citizens and/or Indian companies, which are ultimately owned and controlled by resident Indian citizens;

An entity is considered as '**Owned**' by 'non resident entities', if more than 50% of the capital in it is beneficially owned by non-residents.

**'PAB'** means Project Approval Board in DIPP, Ministry of Commerce & Industry, Government of India.

**'Person'** includes

- (i) an individual,
- (ii) a Hindu undivided family,
- (iii) a company,
- (iv) a firm,
- (v) an association of persons or a body of individuals whether incorporated or not,
- (vi) every artificial juridical person, not falling within any of the preceding subclauses, and
- (vii) any agency, office, or branch owned or controlled by such person.

**'Person of Indian Origin' (PIO)** means a citizen of any country other than Bangladesh or Pakistan, if

- (i) he at any time held Indian Passport
- (ii) he or either of his parents or any of his grandparents was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955 (57 of 1955); or
- (iii) the person is a spouse of an Indian citizen or a person referred to in sub clause (i) or (ii).

**'Person resident in India'** means -

- (i) a person residing in India for more than one hundred and eighty-two days during the course of the preceding financial year but does not include
  - (A) A person who has gone out of India or who stays outside India, in either case--
    - (a) for or on taking up employment outside India, or

- (b) for carrying on outside India a business or vocation outside India, or
  - (c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;
- (B) A person who has come to or stays in India, in either case, otherwise than-
- (a) for or on taking up employment in India; or
  - (b) for carrying on in India a business or vocation in India, or
  - (c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;
- (ii) any person or body corporate registered or incorporated in India,
  - (iii) an office, branch or agency in India owned or controlled by a person resident outside India,
  - (iv) an office, branch or agency outside India owned or controlled by a person resident in India.

**'Person resident outside India'** means a person who is not a Person resident in India.

**'RBI'** means the Reserve Bank of India established under the Reserve Bank of India Act, 1934.

**'Resident Entity'** means 'Person resident in India' excluding an individual.

**'Resident Indian Citizen'** shall be interpreted in line with the definition of 'person resident in India' as per FEMA, 1999, read in conjunction with the Indian Citizenship Act, 1955.

**'SEBI'** means the Securities and Exchange Board of India established under the Securities and Exchange Board of India Act, 1992.

**'SEZ'** means a Special Economic Zone as defined in Special Economic Zone Act, 2005.

**'SIA'** means Secretariat of Industrial Assistance in DIPP, Ministry of Commerce & Industry, Government of India.

**'Transferable Development Rights' (TDR)** means certificates issued in respect of category of land acquired for public purposes either by the Central or State Government in consideration of surrender of land by the owner without monetary compensation, which are transferable in part or whole.

**'Venture Capital Fund' (VCF)** means a Fund established in the form of a Trust, a company including a body corporate and registered under Securities and Exchange Board of India (Venture Capital Fund) Regulations, 1996, which

- (i) has a dedicated pool of capital;
- (ii) raised in the manner specified under the Regulations; and
- (iii) invests in accordance with the Regulations.

## **ORIGIN OF INVESTMENT IN INDIA**

A non-resident entity can invest in India, subject to the FDI Policy. A citizen of Bangladesh or an entity incorporated in Bangladesh can invest in India under the FDI Policy, only under the Government route.

NRIs resident in Nepal and Bhutan as well as citizens of Nepal and Bhutan are permitted to invest in the capital of Indian companies on repatriation basis, subject to the condition that the amount of consideration for such investment shall be paid only by way of inward remittance in free foreign exchange through normal banking channels.

OCBs have been derecognized as a class of Investors in India with effect from September 16, 2003. Erstwhile OCBs which are incorporated outside India and are not under the adverse notice of RBI can make fresh investments under FDI Policy as incorporated non-resident entities, with the prior approval of Government of India if the investment is through Government route; and with the prior approval of RBI if the investment is through Automatic route.

An FII may invest in the capital of an Indian company either under the FDI Scheme/Policy or the Portfolio Investment Scheme. 10% individual limit and 24% aggregate limit for FII investment would be applicable even when FIIs invest under the FDI scheme/policy. The Indian company which has issued shares to FIIs under the FDI Policy for which the payment has been received directly into company's account should report these figures separately under item no. 5 of Form FC-GPR (Post-issue pattern of shareholding) so that the details could be suitably reconciled for statistical/monitoring purposes. A daily statement in respect of all transactions (except derivative trade) have to be submitted by the custodian bank in floppy/soft copy in the prescribed format directly to RBI to monitor the overall ceiling/ sectoral cap/statutory ceiling.

No person other than registered FII/NRI as per Schedules II and III of Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations of FEMA 1999 can invest/trade in capital of Indian Companies in the Indian Stock Exchanges directly i.e. through brokers like a Person Resident in India.

A SEBI registered Foreign Venture Capital Investor (FVCI) may contribute upto 100% of the capital of a Venture Capital Fund/Indian Venture Capital Undertaking and may also set up a domestic asset management company to manage the fund. All such investments are allowed under the automatic route subject to SEBI and RBI regulations and FDI Policy. However FVCIs are also allowed to invest as non-resident entities in other companies subject to FDI Policy.

### **TYPES OF INSTRUMENTS**

Indian companies can issue equity shares, fully, compulsorily and mandatorily convertible debentures and fully, compulsorily and mandatorily convertible preference shares subject to pricing guidelines/valuation norms prescribed under FEMA Regulations. The pricing of the capital instruments should be decided/determined upfront at the time of issue of the instruments.

Other types of Preference shares/Debentures i.e. non-convertible, optionally convertible or partially convertible for issue of which funds have been received on or after May 1, 2007 are considered as debt. Accordingly all norms applicable for ECBs relating to eligible borrowers, recognized lenders, amount and maturity, end-use stipulations, etc. shall apply.

The inward remittance received by the Indian company vide issuance of DRs and FCCBs are treated as FDI and counted towards FDI.

### **Issue of shares by Indian Companies under FCCB/ADR/GDR**

(i) Indian companies can raise foreign currency resources abroad through the issue of FCCB/DR (ADRs/GDRs), in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the Government of India thereunder from time to time.

(ii) A company can issue ADRs/GDRs if it is eligible to issue shares to persons resident outside India under the FDI Policy. However, an Indian listed company, which is not eligible to raise funds from the Indian Capital Market including a company which has been restrained from accessing the securities market by the Securities and Exchange Board of India (SEBI) will not be eligible to issue ADRs/GDRs.

(iii) Unlisted companies, which have not yet accessed the ADR/GDR route for raising capital in the international market, would require prior or simultaneous listing in the domestic market, while seeking to issue such overseas instruments. Unlisted companies, which have already issued ADRs/GDRs in the international market, have to list in the domestic market on making profit or within three years of such issue of ADRs/GDRs, whichever is earlier. ADRs/GDRs are issued on the basis of the ratio worked out by the Indian company in consultation with the Lead Manager to the issue. The proceeds so raised have to be kept abroad till actually required in India. Pending repatriation or utilization of the proceeds, the Indian company can invest the funds in:

- (a) Deposits, Certificate of Deposits or other instruments offered by banks rated by Standard and Poor, Fitch, IBCA, Moody's, etc. with rating not below the rating stipulated by Reserve Bank from time to time for the purpose;
  - (b) Deposits with branch/es of Indian Authorized Dealers outside India; and
  - (c) Treasury bills and other monetary instruments with a maturity or unexpired maturity of one year or less.
- (iv) There are no end-use restrictions except for a ban on deployment/investment of such funds in real estate or the stock market. There is no monetary limit up to which an Indian company can raise ADRs/GDRs.
- (v) The ADR/GDR proceeds can be utilized for first stage acquisition of shares in the disinvestment process of Public Sector Undertakings/Enterprises and also in the mandatory second stage offer to the public in view of their strategic importance.
- (vi) Voting rights on shares issued under the Scheme shall be as per the provisions of Companies Act, 1956 and in a manner in which restrictions on voting rights imposed on ADR/GDR issues shall be consistent with the Company Law provisions. Voting rights in the case of banking companies will continue to be in terms of the provisions of the Banking Regulation Act, 1949 and the instructions issued by the Reserve Bank from time to time, as applicable to all shareholders exercising voting rights.
- (vii) Erstwhile OCBs who are not eligible to invest in India and entities prohibited from buying, selling or dealing in securities by SEBI will not be eligible to subscribe to ADRs/GDRs issued by Indian companies.
- (viii) The pricing of ADR/GDR issues should be made at a price determined under the provisions of the Scheme of issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the Government of India and directions issued by the Reserve Bank, from time to time.
- (ix) The pricing of sponsored ADRs/GDRs would be determined under the provisions of the Scheme of issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the Government of India and directions issued by the Reserve Bank, from time to time.

### **Two-way Fungibility Scheme**

A limited two-way Fungibility scheme has been put in place by the Government of India for ADRs/GDRs. Under this Scheme, a stock broker in India, registered with SEBI, can purchase shares of an Indian company from the market for conversion into ADRs/GDRs based on instructions received from overseas investors. Re-issuance of ADRs/GDRs would be permitted to the extent of ADRs/GDRs which have been redeemed into underlying shares and sold in the Indian market.

### **Sponsored ADR/GDR issue**

An Indian company can also sponsor an issue of ADR/GDR. Under this mechanism, the company offers its

resident shareholders a choice to submit their shares back to the company so that on the basis of such shares, ADRs/GDRs can be issued abroad. The proceeds of the ADR/GDR issue are remitted back to India and distributed among the resident investors who had offered their Rupee denominated shares for conversion. These proceeds can be kept in Resident Foreign Currency (Domestic) accounts in India by the resident shareholders who have tendered such shares for conversion into ADRs/GDRs.

## **ELIGIBILITY OF FDI IN RESIDENT ENTITIES**

### **FDI in an Indian Company**

Indian companies including those which are micro and small enterprises can issue capital against FDI.

### **FDI in Partnership Firm/Proprietary Concern**

- (i) A Non-Resident Indian (NRI) or a Person of Indian Origin (PIO) resident outside India can invest by way of contribution to the capital of a firm or a proprietary concern in India on non-repatriation basis provided;
  - (a) Amount is invested by inward remittance or out of NRE/FCNR(B)/NRO account maintained with Authorized Dealers/Authorized banks.
  - (b) The firm or proprietary concern is not engaged in any agricultural/plantation or real estate business or print media sector.
  - (c) Amount invested shall not be eligible for repatriation outside India.
- (ii) Investments with repatriation benefits: NRIs/PIO may seek prior permission of Reserve Bank for investment in sole proprietorship concerns/partnership firms with repatriation benefits. The application will be decided in consultation with the Government of India.
- (iii) Investment by non-residents other than NRIs/PIO: A person resident outside India other than NRIs/PIO may make an application and seek prior approval of Reserve Bank for making investment by way of contribution to the capital of a firm or a proprietorship concern or any association of persons in India. The application will be decided in consultation with the Government of India.
- (iv) Restrictions: An NRI or PIO is not allowed to invest in a firm or proprietorship concern engaged in any agricultural/plantation activity or real estate business (i.e. dealing in land and immovable property with a view to earning profit or earning income there from) or engaged in Print Media.

### **FDI in Limited Liability Partnership**

FDI in LLPs is permitted, subject to the following conditions:

- (a) FDI in LLPs has been allowed, through the Government approval route, only for LLPs operating in sectors/activities where 100% FDI is allowed, through the automatic route and there are no FDI-linked performance related conditions (such as 'Non Banking Finance Companies' or 'Development of Townships, Housing, Built-up infrastructure and Construction-development projects' etc.)
- (b) LLPs with FDI will not be allowed to operate in agriculture/plantation activity, print media or real estate business.
- (c) An Indian company, having FDI, has been permitted to make downstream investment in an LLP only if both-the company, as well as the LLP- are operating in sectors where 100% FDI is allowed, through the automatic route and there are no FDI-linked performance related conditions.
- (d) LLPs with FDI are not eligible to make any downstream investment.

- (e) Foreign Capital participation in the capital structure of LLPs is allowed only by way of cash consideration, received by inward remittance, through normal banking channels or by debit to NRE/FCNR account of the person concerned, maintained with an authorized dealer/authorized bank.
- (f) Investment in LLPs by Foreign Institutional Investors (FIIs) and Foreign Venture Capital Investors (FVCIs) is not permitted. LLPs are also not permitted to avail External Commercial Borrowings (ECBs)
- (g) In case the LLP with FDI has a body corporate that is a designated partner or nominates an individual to act as a designated partner in accordance with the provisions of Section 7 of the LLP Act, 2008, such a body corporate should only be a company registered in India under the Companies Act, 1956 and not any other body, such as an LLP or a trust.
- (h) For such LLPs, the designated partner “resident in India”, as defined under the ‘Explanation’ to Section 7(1) of the LLP Act, 2008, would also have to satisfy the definition of “person resident in India”, as prescribed under Section 2(v)(i) of the Foreign Exchange Management Act, 1999.
- (i) The designated partners are responsible for compliance with all the above conditions and also liable for all penalties imposed on the LLP for their contravention, if any.
- (j) Conversion of a company with FDI, into an LLP, is allowed only if the above stipulations are met and with the prior approval of the FIPB/Government.

#### FDI in Trusts

FDI in Trusts other than Venture Capital Fund (VCF) is not permitted.

#### ***What is the procedure for receiving Foreign Direct Investment in an Indian company?***

*Ans. An Indian company may receive Foreign Direct Investment under the two routes as given under:*

##### ***i. Automatic Route***

*FDI is allowed under the automatic route without prior approval either of the Government or the Reserve Bank of India in all activities/sectors as specified in the consolidated FDI Policy, issued by the Government of India from time to time.*



##### ***ii. Government Route***

*FDI in activities not covered under the automatic route requires prior approval of the Government which are considered by the Foreign Investment Promotion Board (FIPB), Department of Economic Affairs, Ministry of Finance.*

*The Indian company having received FDI either under the Automatic route or the Government route is required to comply with provisions of the FDI policy including reporting the FDI to the Reserve Bank of India.*

#### CONDITIONS ON ISSUE/TRANSFER OF SHARES

The capital instruments should be issued within 180 days from the date of receipt of the inward remittance or by debit to the NRE/FCNR (B) account of the non-resident investor. In case, the capital instruments are not

issued within 180 days from the date of receipt of the inward remittance or date of debit to the NRE/FCNR (B) account, the amount of consideration so received should be refunded immediately to the non-resident investor by outward remittance through normal banking channels or by credit to the NRE/FCNR (B) account, as the case may be. Non-compliance with the above provision would be reckoned as a contravention under FEMA and would attract penal provisions. In exceptional cases, refund of the amount of consideration outstanding beyond a period of 180 days from the date of receipt may be considered by the RBI, on the merits of the case.

### **Issue price of shares**

Price of shares issued to persons resident outside India under the FDI Policy, shall not be less than -

- (a) the price worked out in accordance with the SEBI guidelines, as applicable, where the shares of the company is listed on any recognised stock exchange in India;
- (b) the fair valuation of shares done by a SEBI registered Category - I Merchant Banker or a Chartered Accountant as per the discounted free cash flow method, where the shares of the company is not listed on any recognised stock exchange in India ; and
- (c) the price as applicable to transfer of shares from resident to non-resident as per the pricing guidelines laid down by the Reserve Bank from time to time, where the issue of shares is on preferential allotment.

### **Foreign Currency Account**

Indian companies which are eligible to issue shares to persons resident outside India under the FDI Policy may be allowed to retain the share subscription amount in a Foreign Currency Account, with the prior approval of RBI.

### **Transfer of shares and convertible debentures**

(i) Subject to FDI sectoral policy, foreign investors can also invest in Indian companies by purchasing/acquiring existing shares from Indian shareholders or from other non-resident shareholders. General permission has been granted to non-residents/NRIs for acquisition of shares by way of transfer subject to the following:

- (a) A person resident outside India (other than NRI and erstwhile OCB) may transfer by way of sale or gift, the shares or convertible debentures to any person resident outside India (including NRIs).
- (b) NRIs may transfer by way of sale or gift the shares or convertible debentures held by them to another NRI.
- (c) A person resident outside India can transfer any security to a person resident in India by way of gift.
- (d) A person resident outside India can sell the shares and convertible debentures of an Indian company on a recognized Stock Exchange in India through a stock broker registered with stock exchange or a merchant banker registered with SEBI.
- (e) A person resident in India can transfer by way of sale, shares/convertible debentures (including transfer of subscriber's shares), of an Indian company under private arrangement to a person resident outside India, subject to the specified guidelines.
- (f) General permission is also available for transfer of shares/convertible debentures, by way of sale under private arrangement by a person resident outside India to a person resident in India, subject to the specified guidelines.
- (g) The above General Permission also covers transfer by a resident to a non-resident of shares/

convertible debentures of an Indian company, engaged in an activity earlier covered under the Government Route but now falling under Automatic Route, as well as transfer of shares by a non-resident to an Indian company under buyback and/or capital reduction scheme of the company.

- (h) The Form FC-TRS should be submitted to the AD Category-I Bank, within 60 days from the date of receipt of the amount of consideration. The onus of submission of the Form FC-TRS within the given timeframe would be on the transferor/transferee, resident in India.
- (ii) The sale consideration in respect of equity instruments purchased by a person resident outside India, remitted into India through normal banking channels, shall be subjected to a Know Your Customer (KYC) check by the remittance receiving AD Category – I bank at the time of receipt of funds. In case, the remittance receiving AD Category – I bank is different from the AD Category – I bank handling the transfer transaction, the KYC check should be carried out by the remittance receiving bank and the KYC report be submitted by the customer to the AD Category – I bank carrying out the transaction along with the Form FC-TRS.
- (iii) Escrow: AD Category – I banks have been given general permission to open Escrow account and Special account of non-resident corporate for open offers/exit offers and delisting of shares. The relevant SEBI (SAST) Regulations or any other applicable SEBI Regulations/provisions of the Companies Act, 1956 will be applicable.

#### **Prior permission of RBI in certain cases for transfer of capital instruments**

The following instances of transfer of capital instruments from resident to non-residents by way of sale require prior approval of RBI:

- (i) Transfer of capital instruments from resident to non-residents by way of sale where:
  - (a) Transfer is at a price which falls outside the pricing guidelines specified by the Reserve Bank from time to time and the transaction does not fall under the specified exception.
  - (b) Transfer of capital instruments by the non-resident acquirer involving deferment of payment of the amount of consideration. Further, in case approval is granted for a transaction, the same should be reported in Form FC-TRS, to an AD Category-I bank for necessary due diligence, within 60 days from the date of receipt of the full and final amount of consideration.
- (ii) A person resident in India, who intends to transfer any capital instrument, by way of gift to a person resident outside India, has to obtain prior approval from Reserve Bank. While forwarding applications to Reserve Bank for approval for transfer of capital instruments by way of gift, the specified documents should be enclosed. Reserve Bank considers the following factors while processing such applications:
  - (a) The proposed transferee (donee) is eligible to hold such capital instruments under Schedules 1, 4 and 5 of Notification No. FEMA 20/2000-RB dated May 3, 2000, as amended from time to time.
  - (b) The gift does not exceed 5 per cent of the paid-up capital of the Indian company/each series of debentures/each mutual fund scheme.
  - (c) The applicable sectoral cap limit in the Indian company is not breached.
  - (d) The transferor (donor) and the proposed transferee (donee) are close relatives as defined in Section 6 of the Companies Act, 1956, as amended from time to time.

- (e) The value of capital instruments to be transferred together with any capital instruments already transferred by the transferor, as gift, to any person residing outside India does not exceed the rupee equivalent of USD 50,000 during the calendar year.
- (f) Such other conditions as stipulated by Reserve Bank in public interest from time to time.

### **Conversion of ECB/Lumpsum Fee/Royalty into Equity**

- (i) Indian companies have been granted general permission for conversion of External Commercial Borrowings (ECB) (excluding those deemed as ECB) in convertible foreign currency into shares/preference shares, subject to the following conditions and reporting requirements.
  - (a) The activity of the company is covered under the Automatic Route for FDI or the company has obtained Government approval for foreign equity in the company;
  - (b) The foreign equity after conversion of ECB into equity is within the sectoral cap, if any;
  - (c) Pricing of shares is as per FDI Policy;
  - (d) Compliance with the requirements prescribed under any other statute and regulation in force; and
  - (e) The conversion facility is available for ECBs availed under the Automatic or Government Route and is applicable to ECBs, due for payment or not, as well as secured/unsecured loans availed from non-resident collaborators.
- (ii) General permission is also available for issue of shares/preference shares against lump sum technical know-how fee, royalty, under automatic route or SIA/FIPB route, subject to pricing guidelines of SEBI/CCI and compliance with applicable tax laws.

### **ISSUE OF INSTRUMENTS**

#### **Issue of Rights/Bonus Shares**

FEMA provisions allow Indian companies to freely issue Rights/Bonus shares to existing non-resident shareholders, subject to adherence to sectoral cap, if any. However, such issue of bonus/rights shares has to be in accordance with other laws/statutes like the Companies Act, 1956, SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (in case of listed companies), etc. The price of shares offered on rights basis by the Indian company to non-resident shareholders shall not be lower than the price at which such shares are offered to resident shareholders.

#### **Prior permission of RBI for Rights issue to erstwhile OCBs**

OCBs have been derecognized as a class of investors from September 16, 2003. Therefore companies desiring to issue rights share to such erstwhile OCBs will have to take specific prior permission from RBI. As such, entitlement of rights share is not automatically available to erstwhile OCBs. However bonus shares can be issued to erstwhile OCBs without the approval of RBI.

#### **Additional allocation of rights share by residents to non-residents**

Existing non-resident shareholders are allowed to apply for issue of additional shares/fully, compulsorily and mandatorily convertible debentures/fully, compulsorily and mandatorily convertible preference shares over and above their rights share entitlements. The investee company can allot the additional rights share out of unsubscribed portion, subject to the condition that the overall issue of shares to non-residents in the total paid-up capital of the company does not exceed the sectoral cap.

### **Acquisition of shares under Scheme of Merger/Demerger/Amalgamation**

Mergers/demergers/amalgamations of companies in India are usually governed by an order issued by a competent Court on the basis of the Scheme submitted by the companies undergoing merger/demerger/amalgamation. Once the scheme of merger or demerger or amalgamation of two or more Indian companies has been approved by a Court in India, the transferee company or new company is allowed to issue shares to the shareholders of the transferor company resident outside India, subject to the conditions that:

- (i) the percentage of shareholding of persons resident outside India in the transferee or new company does not exceed the sectoral cap, and
- (ii) the transferor company or the transferee or the new company is not engaged in activities which are prohibited under the FDI policy .

### **Issue of shares under Employees Stock Option Scheme (ESOPs)**

Listed Indian companies are allowed to issue shares under the Employees Stock Option Scheme (ESOPs), to its employees or employees of its joint venture or wholly owned subsidiary abroad who are resident outside India, other than to the citizens of Pakistan.

ESOPs can be issued to citizens of Bangladesh with the prior approval of FIPB. Shares under ESOPs can be issued directly or through a Trust subject to the condition that:

- (a) The scheme has been drawn in terms of relevant regulations issued by the SEBI, and
- (b) The face value of the shares to be allotted under the scheme to the non-resident employees does not exceed 5 per cent of the paid-up capital of the issuing company.

Unlisted companies have to follow the provisions of the Companies Act, 1956. The Indian company can issue ESOPs to employees who are resident outside India, other than to the citizens of Pakistan. ESOPs can be issued to the citizens of Bangladesh with the prior approval of the FIPB.

The issuing company is required to report the details of such issues to the Regional Office concerned of the Reserve Bank, within 30 days from the date of issue of shares.

## **REMITTANCE AND REPATRIATION**

### **Remittance of sale proceeds:**

Sale proceeds of shares and securities and their remittance is 'remittance of asset' governed by The Foreign Exchange Management (Remittance of Assets) Regulations 2000 under FEMA.

AD Category – I bank can allow the remittance of sale proceeds of a security (net of applicable taxes) to the seller of shares resident outside India, provided the security has been held on repatriation basis, the sale of security has been made in accordance with the prescribed guidelines and NOC/tax clearance certificate from the Income Tax Department has been produced.

### **Remittance on winding up/liquidation of Companies**

AD Category – I banks have been allowed to remit winding up proceeds of companies in India, which are under liquidation, subject to payment of applicable taxes. Liquidation may be subject to any order issued by the court winding up the company or the official liquidator in case of voluntary winding up under the provisions of the Companies Act, 1956. AD Category – I banks shall allow the remittance provided the applicant submits:

- (a) No objection or Tax clearance certificate from Income Tax Department for the remittance.

- (b) Auditor's certificate confirming that all liabilities in India have been either fully paid or adequately provided for.
- (c) Auditor's certificate to the effect that the winding up is in accordance with the provisions of the Companies Act, 1956.
- (d) In case of winding up otherwise than by a court, an auditor's certificate to the effect that there are no legal proceedings pending in any court in India against the applicant or the company under liquidation and there is no legal impediment in permitting the remittance.

### **Repatriation of Dividend**

Dividends are freely repatriable without any restrictions (net after Tax deduction at source or Dividend Distribution Tax, if any, as the case may be). The repatriation is governed by the provisions of the Foreign Exchange Management (Current Account Transactions) Rules, 2000, as amended from time to time.

### **Repatriation of Interest**

Interest on fully, mandatorily and compulsorily convertible debentures is also freely repatriable without any restrictions (net of applicable taxes). The repatriation is governed by the provisions of the Foreign Exchange Management (Current Account Transactions) Rules, 2000, as amended from time to time.

## **FOREIGN DIRECT INVESTMENT REPORTING**

### **Reporting of Inflow**

An Indian company receiving investment from outside India for issuing shares/ convertible debentures/ preference shares under the FDI Scheme, should report the details of the amount of consideration to the Regional Office concerned of the Reserve Bank not later than 30 days from the date of receipt in the Advance Reporting Form.

Indian companies are required to report the details of the receipt of the amount of consideration for issue of shares/convertible debentures, through an AD Category – I bank, together with a copy/ies of the FIRC/s evidencing the receipt of the remittance along with the KYC report on the non-resident investor from the overseas bank remitting the amount. The report would be acknowledged by the Regional Office concerned, which will allot a Unique Identification Number (UIN) for the amount reported.

### **Reporting of issue of shares**

After issue of shares (including bonus and shares issued on rights basis and shares issued under ESOP)/ fully, mandatorily and compulsorily convertible debentures/fully, mandatorily and compulsorily convertible preference shares, the Indian company has to file Form FC-GPR, not later than 30 days from the date of issue of shares.

### **Reporting of transfer of shares**

Reporting of transfer of shares between residents and non-residents and vice- versa is to be done in Form FC-TRS. The Form FC-TRS should be submitted to the AD Category – I bank, within 60 days from the date of receipt of the amount of consideration. The onus of submission of the Form FC-TRS within the given timeframe would be on the transferor/transferee, resident in India. The AD Category – I bank, would forward the same to its link office. The link office would consolidate the Form FC-TRS and submit a monthly report to the Reserve Bank.

### **Reporting of Non-Cash**

Details of issue of shares against conversion of ECB has to be reported to the Regional Office concerned of the RBI, as indicated below:

In case of full conversion of ECB into equity, the company shall report the conversion in Form FC-GPR to the Regional Office concerned of the Reserve Bank as well as in Form ECB-2 to the Department of Statistics and Information Management (DSIM), Reserve Bank of India, Bandra-Kurla Complex, Mumbai – 400 051, within seven working days from the close of month to which it relates. The words "ECB wholly converted to equity" shall be clearly indicated on top of the Form ECB-2. Once reported, filing of Form ECB-2 in the subsequent months is not necessary.

In case of partial conversion of ECB, the company shall report the converted portion in Form FC-GPR to the Regional Office concerned as well as in Form ECB-2 clearly differentiating the converted portion from the non-converted portion. The words "ECB partially converted to equity" shall be indicated on top of the Form ECB-2. In the subsequent months, the outstanding balance of ECB shall be reported in Form ECB-2 to DSIM.

### **Reporting of FCCB/ADR/GDR Issues**

The Indian company issuing ADRs/GDRs has to furnish to the Reserve Bank, full details of such issue in the FORM DR, within 30 days from the date of closing of the issue.

The company should also furnish a quarterly return in the FORM DR-QUARTERLY, to the Reserve Bank within 15 days of the close of the calendar quarter. The quarterly return has to be submitted till the entire amount raised through ADR/GDR mechanism is either repatriated to India or utilized abroad as per the extant Reserve Bank guidelines.

### **Consequences of Violation**

FDI is a capital account transaction and thus any violation of FDI regulations are covered by the penal provisions of the FEMA. Reserve Bank of India administers the FEMA and Directorate of Enforcement under the Ministry of Finance is the authority for the enforcement of FEMA. The Directorate takes up investigation in any contravention of FEMA.

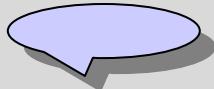
### **Penalties**

If a person violates/contravenes any FDI Regulations, by way of breach/non-adherence/noncompliance/ contravention of any rule, regulation, notification, press note, press release, circular, direction or order issued in exercise of the powers under FEMA or contravenes any conditions subject to which an authorization is issued by the Government of India/FIPB/Reserve Bank of India, he shall, upon adjudication, be liable to a penalty up to thrice the sum involved in such contraventions where such amount is quantifiable, or up to two lakh Rupees where the amount is not quantifiable, and where such contraventions is a continuing one, further penalty which may extend to five thousand Rupees for every day after the first day during which the contraventions continues.

Where a person committing a contravention of any provisions of this Act or of any rule, direction or order made there under is a company (company means any body corporate and includes a firm or other association of individuals as defined in the Companies Act), every person who, at the time the contravention was committed, was in charge of, and was responsible to, the company for the conduct of the business of the company as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly.

Any Adjudicating Authority adjudging any contraventions may, if he thinks fit in addition to any penalty which he may impose for such contravention direct that any currency, security or any other money or property in respect of which the contravention has taken place shall be confiscated to the Central Government.

***FDI is prohibited in the following activities/sectors:***



- *Atomic Energy*
- *Lottery Business including Government/private lottery, online lotteries, etc.*
- *Gambling and Betting including casinos etc.*
- *Business of chit fund*
- *Nidhi company*
- *Trading in Transferable Development Rights (TDRs)*
- *Real Estate Business or Construction of Farm Houses*
- *Activities/sectors not opened to private sector investment.*

***FDI is allowed in the following activities/sectors:***

- Animal Husbandry
- Floriculture
- Pisciculture
- Aquaculture
- Development of seeds
- Vegetable and Mushrooms
- Tea plantation
- Mining
- Manufacture of items reserved for production in Micro and Small Enterprises (MSEs)
- Defence
- Electric Generation, Transmission, Distribution and Trading
- Civil Aviation Sector
- Asset Reconstruction Companies
- Banking – Private Sector
- Banking – Public Sector
- Terrestrial Broadcasting
- Cable network
- DTH
- HITS
- Setting up hardware facilities such as up-linking, HUB
- Commodity Exchange
- Development of Townships, Housing, Built-up infrastructure and Construction-development projects
- Credit Information Companies (CIC)
- Industrial Parks both setting up and in established Industrial Parks
- Insurance
- Infrastructure Company in the Securities Market

- Non-Banking Finance Companies (NBFC)
- Petroleum Refining by PSU
- Print Media
- Security Agencies in Private Sector
- Satellites – Establishment and operation
- Telecommunication
- Ash and Carry Trading Wholesale Trading/Wholesale Trading
- Courier services for carrying packages, parcels and other items which do not come within the ambit of the Indian Post Office Act, 1898
- Trading for export
- E-Commerce Activities
- Trading of items sourced from MSE Sector
- Test Marketing
- Single Brand Product Trading

### **What are the forms in which business can be conducted by a foreign company in India?**

A foreign company planning to set up business operations in India may:

- Incorporate a company under the Companies Act, 1956, as a Joint Venture or a Wholly Owned Subsidiary.
- Set up a Liaison Office / Representative Office or a Project Office or a Branch Office of the foreign company which can undertake activities permitted under the Foreign Exchange Management (Establishment in India of Branch Office or Other Place of Business) Regulations, 2000.



## **DIRECT INVESTMENT OUTSIDE INDIA**

### **What is the significance of overseas direct investments for the country and for the investor?**

*Joint Ventures/Wholly Owned Subsidiaries abroad promote economic co-operation between India and the host countries. They result in transfer of technology and skills, sharing the results of Research & Development, access to the global market, promotion of the brand image, generation of employment and utilization raw materials available in India and the host country, increased exports of plant and machinery and goods and services from India, foreign exchange earnings through dividend earnings, royalty, technical know-how fee, etc. Since globalization of trade is a two-way process, integration of the Indian economy with the rest of the world with all its attendant benefits is achieved through overseas investment. It is the reverse of Foreign Direct Investment (FDI) i.e. Indian direct investment abroad.*



In terms of section 6(3) of FEMA, the Direct investments by residents in Joint Venture (JV) and Wholly Owned Subsidiary (WOS) has been allowed. Section 6(3) of Foreign Exchange Management Act empowers the Reserve Bank to prohibit restrict or regulate various transactions, by making Regulations. In exercise of the above powers, the Reserve Bank has, issued Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004 which has been amended from time to time. The Notification seeks to

regulate acquisition and transfer of a foreign security by a person resident in India i.e. investment by Indian entities in overseas joint ventures and wholly owned subsidiaries as also investment by a person resident in India in shares and securities issued outside India.

### **Prohibitions**

Indian parties are prohibited from making investment in a foreign entity engaged in real estate or banking business.

### **General Permission**

In terms of Regulation 4 general permission has been granted to residents for purchase/acquisition of securities in the following manner:

- (a) out of funds held in RFC account; and
- (b) as bonus shares on existing holding of foreign currency shares.
- (c) when not permanently resident in India, out of their foreign currency resources outside India, General permission is also given to sell the shares so purchased or acquired.

### **Automatic Route**

In terms of Regulation 6 of the Foreign Exchange Management (Transfers or Issue of Foreign Securities Regulation), an Indian party has been permitted to make investment in overseas Joint Ventures (JV)/Wholly Owned Subsidiaries (WOS), not exceeding 400 per cent of the net worth of the Indian party (corporates) as on the date of the last audited balance sheet.

This ceiling will not be applicable where the investment is made out of balances held in Exchange Earners' Foreign Currency account of the Indian party or out of funds raised through ADRs/GDRs.

The above ceiling includes contribution to the capital of the overseas JV/WOS, loan granted to the JV/WOS, and 100 per cent of guarantees issued to or on behalf of the JV/WOS. Such investments are subject to the following conditions:

- (a) The Indian entity may extend loan/guarantee to an overseas concern only in which it has equity participation. Indian entities may offer any form of guarantee - corporate or personal/primary or collateral/guarantee by the promoter company/guarantee by group company, sister concern or associate company in India; provided that
  - (i) All financial commitments including all forms of guarantees are within the overall ceiling prescribed for overseas investment by the Indian party i.e. currently within 400 per cent of the net worth of the Indian party.
  - (ii) No guarantee is 'open ended' i.e. the amount of the guarantee should be specified upfront, and
  - (iii) As in the case of corporate guarantees, all guarantees are required to be reported to Reserve Bank, in Form ODI Part II. Guarantees issued by banks in India in favour of WOSs/JVs outside India, are outside this ceiling and are subject to prudential norms issued by Reserve Bank from time to time.

The Indian party should not be on the Reserve Bank's Exporters caution list/list of defaulters to the banking system circulated by the Reserve Bank/The Credit Information Bureau (India) Ltd (CIBIL) or under investigation by any investigation/ enforcement agency or regulatory body. All transactions relating to a JV/WOS should be routed through one branch of an authorised dealer bank to be designated by the Indian party.

In case of partial/full acquisition of an existing foreign company, where the investment is more than USD 5.00 million, valuation of the shares of the company is required to be made by a Category I Merchant Banker registered with SEBI or an Investment Banker/Merchant Banker outside India registered with the appropriate regulatory authority in the host country; and, in all other cases by a Chartered Accountant or a Certified Public Accountant. However, in cases of investment by way of swap of shares, in all cases irrespective of the amount, valuation of the shares is required to be made by a Category I Merchant Banker registered with SEBI or an Investment Banker outside India registered with the appropriate regulatory authority in the host country. Approval of the Foreign Investment Promotion Board (FIPB) is also a precondition.

In case of investment in overseas JV/WOS abroad by a registered Partnership firm, where entire funding for such investment is done by the firm, it will be in order for individual partners to hold shares for and on behalf of the firm in the overseas JV/ WOS if the host country regulations or operational requirements warrant such holdings.

An Indian party is also permitted to acquire shares of a foreign company engaged in a bonafide business activity, in exchange of ADRs/GDRs issued to the latter in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993, and the guidelines issued there under from time to time by the Central Government, provided:

- (a) ADRs/GDRs are listed on any stock exchange outside India;
- (b) The ADR and/or GDR issue for the purpose of acquisition is backed by underlying fresh equity shares issued by the Indian party;
- (c) The total holding in the Indian entity by persons resident outside India in the expanded capital base, after the new ADR and/or GDR issue, does not exceed the sectoral cap prescribed under the relevant regulations for such investment under FDI;
- (d) Valuation of the shares of the foreign company should be
  - (i) as per the recommendations of the Investment Banker if the shares are not listed on any recognized stock exchange; or
  - (ii) based on the current market Capitalization of the foreign company arrived at on the basis of monthly average price on any stock exchange abroad for the three months preceding the month in which the acquisition is committed and over and above, the premium, if any, as recommended by the Investment Banker in its due diligence report in other cases.

The Indian Party is required to report such acquisition in form ODI to the AD Bank for report to the Reserve Bank within a period of 30 days from the date of the transaction.

It may be noted that Investments in Nepal are permitted only in Indian rupees. Investments in Bhutan are permitted in Indian Rupees as well as in freely convertible currencies. All dues receivable on investments made in freely convertible currencies, as well as their sale/winding up proceeds are required to be repatriated to India in freely convertible currencies only. The automatic route facility is not available for investment in Pakistan.

### **Method of Funding**

Investment in an overseas JV/WOS may be funded out of one or more of the following sources:

- (i) drawal of foreign exchange from an AD Bank in India;
- (ii) capitalisation of exports;
- (ii) swap of shares;

- (iv) utilisation of proceeds of External Commercial Borrowings (ECBs)/Foreign Currency Convertible Bonds (FCCBs);
- (v) in exchange of ADRs/GDRs issued in accordance with the scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993, and the guidelines issued there under from time to time by the Central Government
- (vi) balances held in EEFC account of the Indian party; and
- (vii) utilisation of proceeds of foreign currency funds raised through ADR/GDR issues

In respect of (vi) and (vii) above, the ceiling of 400 per cent of net worth does not apply. However, in respect of investments in the financial sector, they are subject to compliance of Regulation 7 irrespective of the method of funding.

### **Capitalisation of exports and other dues**

- (a) Indian parties are also permitted to capitalise the payments due from the foreign entity towards exports, fees, royalties or any other entitlements due from the foreign entity for supplying technical know-how, consultancy, managerial and other services within the ceilings applicable. Capitalization of Export proceeds remaining unrealized beyond the prescribed period of realization will require the prior approval of the Reserve Bank before capitalisation.
- (b) Indian software exporters are permitted to receive 25 per cent of the value of their exports to an overseas software startup company in the form of shares without entering into Joint Venture Agreements, with prior approval of the Reserve Bank.

### **Investments in Financial Services Sector**

In terms of Regulation 7 an Indian party seeking to make investment in an entity engaged in the financial services sector also is required to fulfill the following additional conditions:

- (i) be registered with the appropriate regulatory authority in India for conducting the financial sector activities;
- (ii) have earned net profit during the preceding three financial years from the financial services activities;
- (iii) have obtained approval for investment in financial sector activities abroad from regulatory authorities concerned in India and abroad; and
- (iv) have fulfilled the prudential norms relating to capital adequacy as prescribed by the regulatory authority concerned in India.

A step down subsidiary of JV/WOS investing in a financial services sector is also required to comply with the above conditions.

Regulated entities in the financial sector making investments in any activity overseas are required to comply with the above guidelines. It is clarified that unregulated entities in the financial services sector in India may invest in non financial sector activities subject to compliance with the provisions of Regulation 6. It is further clarified that trading in Commodities Exchanges overseas and setting up JV/WOS for trading in overseas exchanges are reckoned as financial services activity and require clearance from the Forward Markets Commission.

## Investment in Equity of Companies Registered Overseas/Rated Debt Instruments

### **Corporates**

Listed Indian companies are permitted to invest abroad in companies listed on a recognized stock exchange. Such investments should not exceed 50 per cent of the Indian company's net worth as on the date of the latest audited balance sheet.

### **Individuals**

Resident individuals are permitted to invest in equity and in rated bonds/fixed income securities of overseas companies as permitted in terms of the limits and conditions specified under the Liberalised Remittance Scheme.

### **Investment by Mutual Funds**

Mutual Funds are permitted to invest in ADRs/GDRs of the Indian and foreign companies, rated debt instruments, equity of listed overseas companies, ETFs and overseas mutual funds that make nominal investments (i.e., to the extent of 10 per cent of net asset value) in unlisted overseas securities. Domestic Venture Capital Funds registered with SEBI may invest in equity and equity linked instruments of off-shore Venture Capital Undertakings, subject to an overall limit of USD 500 million.

### **Approval of the Reserve Bank**

Prior approval of the Reserve Bank is required in all other cases of direct investment abroad. For this purpose, application together with necessary documents should be made in Form ODI submitted through their Authorised Dealer. Reserve Bank, takes into account the following factors while considering such applications:

- (a) Prima facie viability of the JV/WOS outside India;
- (b) Contribution to external trade and other benefits which will accrue to India through such investment;
- (c) Financial position and business track record of the Indian party and the foreign entity;
- (d) Expertise and experience of the Indian party in the same or related line of activity of the JV/WOS outside India

### **Overseas Investments by Proprietorship Concerns**

With a view to enabling recognized star exporters with a proven track record and a consistently high export performance to reap the benefits of globalization and liberalization, proprietorship concerns and unregistered partnership firms have been allowed to set up a JV/WOS outside India with prior approval of the Reserve Bank subject to satisfying certain eligibility criteria.

An application in form ODI may be made to the Chief General Manager, Reserve Bank of India, Foreign Exchange Department, Overseas Investment Division, Central Office, Amar Building 3rd Floor, Fort, Mumbai 400 001, through the AD Banks.

Investments by established proprietorship or unregistered partnership exporter firms is subject to the following criteria:

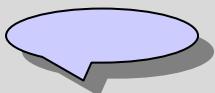
- (i) The Partnership/Proprietorship firm is a DGFT recognized Star Export House (export exceeding Rs.15 crore) per annum.

- (ii) The AD bank is satisfied that the exporter is KYC (Know Your Customer) compliant, is engaged in the proposed business and has turnover as indicated.
- (iii) Exporter has proven track record i.e. export outstanding does not exceed 10 per cent of the average export realization of preceding three financial years.
- (iv) The exporter has not come under adverse notice of any Government agency like Enforcement Directorate, CBI and does not appear in the exporters' caution list of the Reserve Bank or in the list of defaulters to the banking system in India.
- (v) The amount of investment outside India does not exceed 10 per cent of the average of three financial years export realization or 200 per cent of the net owned funds of the firm, whichever is lower.

### **Overseas Investment by Registered Trust/Society**

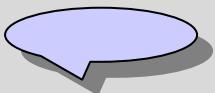
Registered Trusts and Societies engaged in manufacturing/educational sector are allowed make investment in the same sector(s) in a Joint Venture or Wholly Owned Subsidiary outside India, with the prior approval of the Reserve Bank. Trusts/ Societies satisfying the eligibility criteria as given below may submit the application/s in Form ODI-Part I, through their Authorised Dealer.

#### ***Eligibility Criteria for Trust :***



- *The Trust should be registered under the Indian Trust Act, 1882;*
- *The Trust deed permits the proposed investment overseas;*
- *The proposed investment should be approved by the trustee/s;*
- *Authorised Dealer Bank is satisfied that the Trust is KYC (Know Your Customer) compliant and is engaged in a bonafide activity;*
- *The Trust has been in existence at least for a period of three years;*
- *The Trust has not come under the adverse notice of any Regulatory/ Enforcement agency like the Directorate of Enforcement, CBI etc.*

#### ***Eligibility Criteria for Society :***



- *The Society should be registered under the Societies Registration Act, 1860.*
- *The Memorandum of Association and rules and regulations permit the Society to make the proposed investment which should also be approved by the governing body/council or a managing/executive committee.*
- *The AD Category-I bank is satisfied that the Society is KYC (Know Your Customer) compliant and is engaged in a bonafide activity;*
- *The Society has been in existence at least for a period of three years;*
- *The Society has not come under the adverse notice of any Regulatory/ Enforcement agency like the Directorate of Enforcement, CBI etc.*

In addition to the registration, the activities which require special license/ permission either from the Ministry of Home Affairs, Government of India or from the relevant local authority, as the case may be, the Authorised Dealer Bank should ensure that such special license/permission has been obtained by the applicant, sale of securities so acquired.

### **Acquisition of a foreign company through bidding or tender procedure**

In terms of Regulation 14 an Indian party may remit earnest money deposit or issue a bid bond guarantee for acquisition of a foreign company through bidding and tender procedure and also make subsequent remittances through an AD Bank .

### **Obligations of Indian Entity**

In terms of provisions of Regulation 15 an Indian party which has made direct investment abroad has been put under obligation to (a) receive share certificate or any other document as an evidence of investment, (b) repatriate to India the dues receivable from foreign entity and (c) submit the documents/Annual Performance Report to the Reserve Bank, in accordance with the provisions specified in Regulation 15 of the Notification.

### **Transfer by way of sale of shares of a JV/WOS Involving Write Off of the Investment**

Indian parties may also disinvest without prior approval of the Reserve Bank, in the following categories:

- (i) in case where the JV/WOS is listed in the overseas stock exchange;
- (ii) in cases where the Indian party company is listed on a stock exchange in India and has a net worth of not less than ₹100 crore;
- (iii) where the Indian party is an unlisted company and the investment in overseas venture does not exceed USD 10 million.
- (iv) where the Indian Party is a listed company with the net worth of less than ₹100 crore but investment in an overseas JV/WOS does not exceed USD 10 million.

The Indian entity is required to submit details of the disinvestment through its designated Authorised Dealer bank within 30 days from the date of investment. An Indian party, which does not satisfy the conditions laid down, shall have to apply to the Reserve Bank for prior permission.

### **Permission for purchase/acquisition of foreign securities in certain cases**

General permission has been granted to a person resident in India who is an individual–

- (a) to acquire foreign securities as a gift from any person resident outside India; or
- (b) to acquire shares under Cashless Employees Stock Option Scheme issued by a company outside India, provided it does not involve any remittance from India; or
- (c) to acquire shares by way of inheritance from a person whether resident in or outside India;
- (d) to purchase equity shares offered by a foreign company under its ESOP Schemes if he is an employee, or, a director of an Indian office or branch of a foreign company, or, of a subsidiary in India of a foreign company, or, an Indian company in which foreign equity holding, either direct or through a holding company/Special Purpose Vehicle (SPV), is not less than 51 per cent.

A person resident in India may transfer by way of sale the shares acquired as stated above provided that the proceeds thereof are repatriated immediately on receipt thereof and in any case not later than 90 days from the date of sale of such securities.

- (e) Foreign companies are permitted to repurchase the shares issued to residents in India under any ESOP Scheme provided (i) the shares were issued in accordance with the Rules/Regulations framed under Foreign Exchange Management Act, 1999, (ii) the shares are being repurchased in terms of the initial offer document and, (iii) An annual return is submitted through the AD Bank giving details of remittances/beneficiaries, etc.
- (f) In all other cases, not covered by general or special permission, approval of the Reserve Bank is required to be obtained before acquisition of a foreign security.

### **Pledge of a foreign security by a person resident in India**

The shares acquired by persons resident in India in accordance with the provisions of Foreign Exchange Management Act, 1999 or Rules or Regulations made thereunder are allowed to be pledged for obtaining credit facilities in India from an AD Bank/Public Financial Institution.

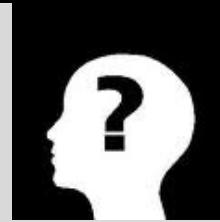
### **General permission in certain cases**

Residents are permitted to acquire a foreign security, if it represents –

- (a) qualification shares for becoming a director of a company outside India to the extent prescribed as per the law of the host country where the company is located provided it does not exceed the limit prescribed for the resident individuals under the Liberalized Remittance Scheme (LRS) in force at the time of acquisition;
- (b) part/full consideration of professional services rendered to the foreign company or in lieu of Director's remuneration. The limit of acquiring such shares in terms of value is restricted to the overall ceiling prescribed for the resident individuals under the Liberalized Remittance Scheme (LRS) in force at the time of acquisition;
- (c) purchase of shares of a JV/WOS abroad of the Indian promoter company by the employees/directors of Indian promoter company which is engaged in the field of software where the consideration for purchase does not exceed USD 10,000 or its equivalent per employee in a block of five calendar years; the shares so acquired do not exceed 5 per cent of the paid-up capital of the JV/WOS outside India; and after allotment of such shares, the percentage of shares held by the Indian promoter company, together with shares allotted to its employees is not less than the percentage of shares held by the Indian promoter company prior to such allotment;
- (d) purchase of foreign securities under ADR/GDR linked stock option schemes by resident employees of Indian companies in the knowledge based sectors, including working directors provided purchase consideration does not exceed USD 50,000 or its equivalent in a block of five calendar years.

### **What is direct investment outside India?**

*Direct investment outside India means investment by way of contribution to the capital or subscription to the Memorandum of Association of a foreign entity, signifying a long term interest (setting up a Joint Venture (JV) or a Wholly Owned Subsidiary (WOS)) in the overseas entity and thus does not include portfolio investment.*



### **ACQUISITION AND TRANSFER OF IMMOVABLE PROPERTY OUTSIDE INDIA**

The Reserve Bank of India in exercise of the powers conferred under Section 6(3)(h) and Section 47(2) of the Foreign Exchange Management Act, 1999 prescribed regulations in respect of acquisition and transfer of immovable property outside India.

A person resident in India is prohibited from acquiring or transferring any immovable property situated outside India without general or special permission of the Reserve Bank. However, this prohibition is not applicable to the property held by a person resident in India who is a national of a foreign state; and acquired by a person resident in India on or before 8th July, 1947 and continued to be held by him with the permission of the Reserve Bank.

A person resident in India may acquire immovable property outside India by way of gift or inheritance from a person who was resident outside India, in terms of Section 6(4) of FEMA acquired by a person resident in India on or before July 8, 1947 and continued to be held by him with the permission of RBI.

A person resident in India may acquire immovable property outside India by way of purchase out of foreign exchange held in Resident Foreign Currency (RFC) account maintained in accordance with the Foreign Exchange Management (Foreign Currency Accounts by a person resident in India) Regulations, 2000.

Reserve Bank is empowered to permit a company incorporated in India having overseas offices, to acquire immovable property outside India for its business and for residential purpose of its staff subject to such terms and conditions as it considers necessary.

A person resident in India who has acquired immovable property outside India as above may transfer it by way of gift to his relative who is a person resident in India. For this purpose, relative in relation to an individual means husband, wife, brother or sister or any lineal ascendant or descendant of that individual.

### **ACQUISITION AND TRANSFER OF IMMOVABLE PROPERTY IN INDIA**

The Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2000, issued by the RBI defines the term 'A person of Indian origin' as to mean an individual (not being a citizen of Pakistan or Bangladesh or Sri Lanka or Afghanistan or China or Iran or Nepal or Bhutan), who

- (i) at any time, held Indian passport; or
- (ii) who or either of whose father or whose grandfather was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955.

The term 'Repatriation outside India' has been defined to mean the buying or drawing of foreign exchange from an authorised dealer in India and remitting it outside India through normal banking channels or crediting it to an account denominated in foreign currency or to an account in Indian currency maintained with an authorised dealer from which it can be converted in foreign currency.

### ***Acquisition and Transfer of Property in India by an Indian Citizen Resident Outside India***

An Indian citizen resident outside India may—

- (i) acquire any immovable property in India other than agricultural/plantation/ farm house,
- (ii) transfer any immovable property in India to a person resident in India, and
- (iii) transfer any immovable property other than agricultural or plantation property or farm house to an Indian citizen or to a person of Indian origin, resident outside India.

### ***Acquisition and Transfer of Property in India by a Person of Indian Origin***

A person of Indian origin resident outside India may acquire any immovable property other than agricultural land/farm house/ plantation property in India by purchase, from out of funds received in India through normal banking channels by way of inward remittance from any place outside India or funds held in any non-resident account maintained in accordance with the provisions of the Act and the regulations made by the Reserve Bank under the Act. It has been clarified that such payments can not be made either by traveller's cheque or

by foreign currency notes or by other mode other than those specified in this behalf. He may also acquire any immovable property in India other than agricultural land/farm house/plantation property by way of gift from a person resident in India or from a person resident outside India who is a citizen of India or from a person of Indian origin resident outside India.

A person of Indian origin resident outside may also acquire any immovable property in India by way of inheritance from a person resident outside India who had acquired such property in accordance with the provisions of the foreign exchange law in force at the time of acquisition by him or the provisions of these Regulations or from a person resident in India. He has been permitted to transfer any immovable property in India other than agricultural land/farm house/plantation property, by way of sale to a person resident in India; transfer agricultural land/farm house/plantation property in India, by way of gift or sale to a person resident in India who is a citizen of India; and transfer residential or commercial property in India by way of gift to a person resident in India or to a person resident outside India who is a citizen of India or to a person of Indian origin resident outside India.

#### ***Acquisition of Immovable Property for Carrying on a Permitted Activity***

A person resident outside India who has established in India in accordance with the Foreign Exchange Management (Establishment in India of Branch or Office or other Place of Business) Regulations, 2000, a branch, office or other place of business for carrying on in India any activity, except a liaison office, may acquire any immovable property in India, which is necessary for or incidental to carrying on such activity, provided that all applicable laws, rules, regulations or directions for the time being in force are duly complied with; and the person files with the Reserve Bank a declaration in the Form IPI not later than ninety days from the date of such acquisition. Such a person is also allowed to transfer by way of mortgage to an authorised dealer as a security for any borrowing, the acquired immovable property.

#### ***Purchase/Sale of Immovable Property by Foreign Embassies/Diplomats/Consulate Generals***

A Foreign Embassies/Diplomats/Consulate Generals may purchase/sell immovable property in India other than agricultural land/farm house/plantation property provided (i) clearance from government of India, Ministry of External Affairs is obtained for such purchase/sale and (ii) the consideration for acquisition of immovable property in India is paid out of funds remitted from abroad through banking channel.

#### ***Repatriation of Sale Proceeds***

A person resident outside India, or his successor shall not, except with the prior permission of the Reserve Bank, repatriate outside India the sale proceeds of any immovable property. In the event of sale of immovable property other than agricultural land/farm house/plantation property in India by a person resident outside India who is a citizen of India or a person of Indian origin, the authorised dealer may allow repatriation of the sale proceeds outside India, provided the following conditions are satisfied—

- (a) the immovable property was acquired by the seller in accordance with the provisions of the foreign exchange law in force at the time of acquisition by him or the provisions of Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2000;
- (b) the amount to be repatriated does not exceed the amount paid for acquisition of the immovable property in foreign exchange received through normal banking channels or out of funds held in Foreign Currency Non-Resident Account or the foreign currency equivalent, as on the date of payment, of the amount paid where such payment was made from the funds held in Non-Resident External account for acquisition of the property.
- (c) In the case of residential property, the repatriation of sale proceeds is restricted to not more than two such properties.

### **Who can purchase immovable property in India ?**

Under the general permission available, the following categories can purchase immovable property in India:

- (i) Non-Resident Indian (NRI)
- (ii) Person of Indian Origin (PIO)



The general permission, however, covers only purchase of residential and commercial property and is not available for purchase of agricultural land / plantation property / farm house in India.

## **ESTABLISHMENT IN INDIA OF BRANCH/LIAISON/PROJECT OFFICE**

Establishment of Branch/Liaison /Project Offices in India is regulated in terms of Section 6(6) of Foreign Exchange Management Act, 1999 read with Foreign Exchange Management (Establishment in India of branch or office or other place of business) Regulations, 2000 as amended from time to time.

A body corporate incorporated outside India (including a firm or other association of individuals), desirous of opening a Liaison Office (LO) / Branch Office (BO) in India have to obtain permission from the Reserve Bank under provisions of FEMA 1999. The applications from such entities considered by Reserve Bank under two routes:

- **Reserve Bank Route** — Where principal business of the foreign entity falls under sectors where 100 per cent Foreign Direct Investment (FDI) is permissible under the automatic route.
- **Government Route** — Where principal business of the foreign entity falls under the sectors where 100 per cent FDI is not permissible under the automatic route. Applications from entities falling under this category and those from Non - Government Organisations / Non - Profit Organisations / Government Bodies / Departments are considered by the Reserve Bank in consultation with the Ministry of Finance, Government of India.

The following additional criteria are also considered by the Reserve Bank while sanctioning Liaison/Branch Offices of foreign entities:

- **Track Record**
  - **For Branch Office** — a profit making track record during the immediately preceding five financial years in the home country.
  - **For Liaison Office** — a profit making track record during the immediately preceding three financial years in the home country.
- **Net Worth** [total of paid-up capital and free reserves, less intangible assets as per the latest Audited Balance Sheet or Account Statement certified by a Certified Public Accountant or any Registered Accounts Practitioner by whatever name].
  - For Branch Office — not less than USD 100,000 or its equivalent.
  - For Liaison Office — not less than USD 50,000 or its equivalent.

### **Permissible Activities for a Liaison Office**

A Liaison Office (also known as Representative Office) can undertake only liaison activities, i.e. it can act as a channel of communication between Head Office abroad and parties in India. It is not allowed to undertake

any business activity in India and cannot earn any income in India. Expenses of such offices are to be met entirely through inward remittances of foreign exchange from the Head Office outside India. The role of such offices is, therefore, limited to collecting information about possible market opportunities and providing information about the company and its products to the prospective Indian customers. Permission to set up such offices is initially granted for a period of 3 years and this may be extended from time to time by an AD Category I bank.

#### ***Liaison Office can undertake the following activities in India:***

- Representing in India the parent company / group companies.
- Promoting export / import from / to India.
- Promoting technical/financial collaborations between parent/group companies and companies in India.
- Acting as a communication channel between the parent company and Indian companies.

#### **Liaison Office of Foreign Insurance Companies / Banks**

Foreign Insurance companies can establish Liaison Offices in India only after obtaining approval from the Insurance Regulatory and Development Authority (IRDA). Foreign banks can establish Liaison Offices in India only after obtaining approval from the Department of Banking Operations and Development (DBOD), Reserve Bank of India.

#### **Permissible Activities for branch offices**

Companies incorporated outside India and engaged in manufacturing or trading activities are allowed to set up Branch Offices in India with specific approval of the Reserve Bank. Such Branch Offices are permitted to represent the parent / group companies and undertake the following activities in India:

- Export / Import of goods.
- Rendering professional or consultancy services.
- Carrying out research work, in areas in which the parent company is engaged.
- Promoting technical or financial collaborations between Indian companies and parent or overseas group company.
- Representing the parent company in India and acting as buying / selling agent in India.
- Rendering services in information technology and development of software in India.
- Rendering technical support to the products supplied by parent/group companies.
- Foreign airline / shipping company.

Normally, the Branch Office should be engaged in the activity in which the parent company is engaged.

#### **Branch Office in Special Economic Zones (SEZs)**

Reserve Bank has given general permission to foreign companies for establishing branch/unit in Special Economic Zones (SEZs) to undertake manufacturing and service activities. The general permission is subject to the following conditions:

- such units are functioning in those sectors where 100 per cent FDI is permitted;
- such units comply with part XI of the Companies Act,1956 (Section 592 to 602);
- such units function on a stand-alone basis.

In the event of winding-up of business and for remittance of winding-up proceeds, the branch shall approach an AD Category – I bank with the documents as mentioned under "Closure of Liaison / Branch Office" except the copy of the letter granting approval by the Reserve Bank.

### **Project office**

Reserve Bank has granted general permission to foreign companies to establish Project Offices in India, provided they have secured a contract from an Indian company to execute a project in India, and

- the project is funded directly by inward remittance from abroad; or
- the project is funded by a bilateral or multilateral International Financing Agency; or
- the project has been cleared by an appropriate authority; or
- a company or entity in India awarding the contract has been granted Term Loan by a Public Financial Institution or a bank in India for the project.

However, if the above criteria are not met, the foreign entity has to approach the Reserve Bank of India for approval.

### ***What are the permitted activities of Liaison Office/ Representative Office?***

*Liaison Office (also known as Representative Office) can undertake only liaison activities, i.e. it can act as a channel of communication between Head Office abroad and parties in India. It is not allowed to undertake any business activity in India and cannot earn any income in India. Expenses of such offices are to be met entirely through inward remittances of foreign exchange from the Head Office outside India. The role of such offices is, therefore, limited to collecting information about possible market opportunities and providing information about the company and its products to the prospective Indian customers. A Liaison Office can undertake the following activities in India:*



- (i) Representing in India the parent company / group companies.
- (ii) Promoting export / import from / to India.
- (iii) Promoting technical/financial collaborations between parent/group companies and companies in India.
- (iv) Acting as a communication channel between the parent company and Indian companies.

## **EXPORT OF GOODS AND SERVICES**

Section 7 of the Act deals with export of goods and services. Under Sub-section (1) every exporter is required to furnish to Reserve Bank or any other authority as prescribed, a declaration containing true and correct particulars, including the amount representing the full export value or if the full export value of the goods is not ascertainable at the time of export, the value which the exporter having regard to prevailing market conditions expects to receive on sale of the goods in a market outside India. Every exporter is also under obligation to furnish such other information as may be required by the Reserve Bank for the purpose of ensuring the realisation of the export proceeds.

### **Declaration as Regards Export of Goods and Services**

Every exporter of goods or software, in physical form or through any other form either directly or indirectly to any place outside India, other than Nepal and Bhutan, is required to furnish to the specified authority a

declaration in the prescribed form and supported by specified evidence containing true and correct material particulars including the amount representing the full export value of the goods or software or if the full export value is not ascertainable at the time of export, the value which the exporter having regard to the prevailing market conditions expects to receive on the sale of goods or the software in the overseas market, affirming that the full export value of goods (whether ascertainable at the time of export or not) or the software has been or will within the specified period be paid in the specified manner.

In respect of export of services to which none of the forms specified apply, the exporter may export such services without furnishing any declaration, but shall be liable to realise the amount of foreign exchange which becomes due or accrues on account of such export and to repatriate the same to India.

### **Export of Goods or Services Without Declaration**

Export of goods or services may be made without furnishing the declaration in the following cases, namely:

- (i) trade samples of goods and publicity material supplied free of cost;
- (ii) personal effects of travellers, whether accompanied or unaccompanied;
- (iii) ships stores, trans-shipment cargo and goods supplied under the orders of Central Government or of such officers as may be appointed by the Central Government in this behalf or of the military, naval or air force authorities in India for military, naval or air force requirements;
- (iv) goods or software accompanied by a declaration by the exporter that they are not more than twenty five thousand rupees in value;
- (v) by way of gift of goods accompanied by a declaration by the exporter that they are not more than one lakh rupees in value;
- (vi) aircrafts or aircraft engines and spare parts for overhauling and/or repairs abroad subject to their reimport into India after overhauling/repairs, within a period of six months from the date of their export;
- (vii) goods imported free of cost on re-export basis;
- (viii) goods not exceeding US\$ 1000 or its equivalent in value per transaction exported to Myanmar under the Barter Trade Agreement between the Central Government and the Government of Myanmar;
- (ix) the goods which are permitted by the Development Commissioner of the Export Processing Zones, EHTP, STP or Free Trade Zones to be re-exported. These include, imported goods found defective, for the purpose of their replacement by the foreign suppliers/collaborators; goods imported from foreign suppliers/collaborators on loan basis; goods imported from foreign suppliers/collaborators free of cost, found surplus after production operations. These goods may also be re-exported by the units in SEZ, under the intimation to Development Commissioner of SEZ/concerned Asstt. Commissioner or Dy. Commissioner of customs.
- (x) replacement goods exported free of charge in accordance with the provisions of Exim Policy in force, for the time being.
- (xi) goods sent outside India for testing subject to re-import into India.
- (xii) defective goods sent outside India for repair and re-import provided the goods are accompanied by a certificate from authorised dealer in India that the export is for repair and re-import and that the export does not involve any transaction in foreign exchange.
- (xiii) export permitted by RBI.

### **Indication of Importer-Exporter Code Number**

The importer-exporter code number allotted by the Director General of Foreign Trade under Section 7 of the Foreign Trade (Development and Regulation) Act, 1992 has to be indicated on all copies of the declaration forms submitted by the exporter to the specified authority and also in all correspondence with the authorised dealer or the Reserve Bank, as the case may be.

### **Evidence in Support of Declaration**

The Commissioner of Customs or the postal authority or the official of Department of Electronics, to whom the declaration form is submitted, may, in order to satisfy themselves of due compliance of provisions of the Act and the regulations made thereunder require such evidence in support of the declaration as may establish that the exporter is a person resident in India and has a place of business in India; and the destination stated on the declaration is the final place of the destination of the goods exported.

The term 'final place of destination has been defined to mean a place in a country in which the goods are ultimately imported and cleared through Customs of that country; and the value stated in the declaration represents the full export value of the goods or software; or where the full export value of the goods or software is not ascertainable at the time of export the value which the exporter, having regard to the prevailing market conditions expects to receive on the sale of the goods in the overseas market.

### **Manner of Payment of Export Value of Goods**

Unless otherwise authorised by the Reserve Bank, the amount representing the full export value of the goods exported shall be paid through an authorised dealer in the manner specified in the Foreign Exchange Management (Manner of Receipt and Payment) Regulations, 2000. In this context, the re-import into India, within the period specified for realisation of the export value of the exported goods in respect of which a declaration was made, shall be deemed to be realisation of full export value of such goods.

### **Time Limit for Realisation of Export Value of Goods/Software**

The amount representing the full export value of goods or software exported is required to be realised and repatriated to India within twelve months from the date of export. However where the goods or software are exported by the units in Special Economic Zones, the stipulation of period of realization and repatriation to India of full export value of goods or software shall not apply. In the case of export of goods to a warehouse established outside India with the permission of the Reserve Bank, the amount representing the full export value of goods exported is to be paid to the authorised dealer as soon as it is realised and in any case within fifteen months from the date of shipment of goods. In this regard the authorised dealer have been empowered, for a sufficient and reasonable cause shown, to extend the said period of twelve months or fifteen months as the case may be.

However, in the case of export of goods or software by a statusholder exporter, the amount representing full export value of goods or software shall be realised within a period of twelve months from the date of export. In this context, RBI has been empowered to extend the said period of twelve months.

No person shall enter into any contract, without the approval of RBI, to export goods on the terms which provide for a period longer than twelve months for payment of the value of the goods to be exported.

### **Submission of export documents**

The documents pertaining to export shall, within 21 days from the date of export as, as the case may be, from the date of certification of SOFTEX form, be submitted to the Authorised Dealer mentioned in the

relevant declaration form. However, subject to the directions issued by the Reserve Bank from time to time, the Authorised Dealer may accept the documents pertaining to export submitted after the expiry of the specified period of 21 days, for reasons beyond the control of the exporter.

### **Transfer of Documents**

Regulation 12 empowers the authorised dealer to accept, for negotiation or collection, shipping documents including invoice and bill of exchange covering exports, from his constituent not being a person who has signed the declaration as regards to export of goods and services. However where the value declared in the declaration does not differ from the value shown in the documents being negotiated or sent for collection, or where the value declared in the declaration is less than the value shown in the documents being negotiated or sent for collection, the authorised dealer, before accepting the documents, require the constituent concerned also to sign such declaration and thereupon such constituent shall be bound to comply with such requisition and such constituent signing the declaration shall be considered to be the exporter to the extent of the full value shown in the documents being negotiated or sent for collection.

### **Payment for the Export**

In respect of export of any goods or software requiring a declaration to be furnished, no person shall, without the permission of the Reserve Bank or, subject to the directions of the Reserve Bank, do or refrain from doing anything or take or refrain from taking any action which has the effect of securing that the payment for the goods or software is made otherwise than in the specified manner; or that the payment is delayed beyond the specified period; or that the proceeds of sale of the goods or software exported do not represent the full export value of the goods or software subject to such deductions, if any, as may be allowed by the Reserve Bank or, subject to the directions of the Reserve Bank, by an authorised dealer.

However, proceedings in respect of contravention of these provisions shall not be instituted unless the specified period has expired and payment for the goods or software representing the full export value, or the value after allowed deductions, has not been made in the specified manner within the specified period.

### **Certain Exports Requiring Prior Approval**

Regulation 14 of the Foreign Exchange Management (Export of Goods and Services) Regulation, 2000 requires certain exports to obtain prior approval of Reserve Bank.

#### **(a) Export of Goods on Lease, Hire, etc.**

No person is allowed, except with the prior permission of the Reserve Bank, to take or send out by land, sea or air any goods from India to any place outside India on lease or hire or under any arrangement or in any other manner other than sale or disposal of such goods.

#### **(b) Exports under Trade Agreement/Rupee Credit etc.**

Export of goods under special arrangement between the Central Government and Government of a foreign state, or under rupee credits extended by the Central Government to Government of a foreign state are governed by the terms and conditions set out in the relative public notices issued by the Trade Control Authority in India and the instructions issued from time to time by the Reserve Bank.

The export under the line of credit extended to a bank or a financial institution operating in a foreign state by the Exim Bank for financing exports from India, are governed by the terms and conditions advised by the Reserve Bank to the authorised dealers from time to time.

**(c) Counter Trade**

Any arrangement involving adjustment of value of goods imported into India against value of goods exported from India, requires prior approval of the Reserve Bank.

**Delay in Receipt of Payment**

Where in relation to goods or software export of which is required to be declared on the specified form, the specified period has expired and the payment therefor has not been made as aforesaid, the Reserve Bank may give to any person who has sold the goods or software or who is entitled to sell the goods or software or procure the sale thereof, such directions as appear to it to be expedient, for the purpose of securing,

- (a) the payment therefor if the goods or software has been sold and
- (b) the sale of goods and payment thereof, if goods or software has not been sold or re-import thereof into India as the circumstances permit, within such period as the Reserve Bank may specify in this behalf ;

However, omission of the Reserve Bank to give directions shall not have the effect of absolving the person committing the contravention from the consequences thereof.

**Advance payment against exports**

Where an exporter receives advance payment (with or without interest), from a buyer outside India, the exporter has been put under an obligation to ensure that -

- (i) The shipment of goods is made within one year from the date of receipt of advance payment;
- (ii) The rate of interest, if any, payable on the advance payment does not exceed London Inter-Bank Offered Rate (LIBOR) + 100 basis points, and

The documents covering the shipment are routed through the Authorised Dealer through whom the advance payment is received.

However, in the event of the exporter's inability to make the shipment, partly or fully, within one year from the date of receipt of advance payment, no remittance towards refund of unutilised portion of advance payment or towards payment of interest, shall be made after the expiry of the said period of one year, without the prior approval of the Reserve Bank. In case the export agreement provides for shipment of goods extending beyond the period of one year from the date of receipt of advance payment, the exporter shall require the prior approval of the Reserve Bank.

**Project exports**

Regulation 18 deals with project exports and provides that where the export of goods or services is proposed to be made on deferred payment terms or in execution of a turnkey project or a civil construction contract, the exporter shall, before entering into any such export arrangement, submit the proposal for prior approval of the Working Group, or the Exim Bank or Authorised dealer, as the case may be, which shall consider the proposal in accordance with the guidelines issued by the Reserve Bank from time to time.

**REALISATION, REPATRIATION AND HOLDING OF FOREIGN CURRENCY**

Section 8 of the Act requires the person resident in India to make all reasonable efforts to realise and repatriate the foreign exchange due or accrued as per the directions of the Reserve Bank.

Foreign Exchange Management (Realisation, Repatriation and Surrender of Foreign Exchange) Regulations,

2000 requires a person resident in India to whom any foreign exchange is due or has accrued, to take all reasonable steps to realise and repatriate to India such foreign exchange unless an exemption has been granted under the Act and rules or regulations made thereunder or under the general or special permission of Reserve Bank. Regulation 3 also requires a person resident in India, to refrain from doing anything/taking any action, resulting in delay in receipt of foreign exchange in whole or part, or ceasing in whole or part the foreign exchange receivable by him.

### **Manner of Repatriation**

Regulation 4 requires that after realisation of foreign exchange due, the person concerned shall repatriate the same to India and sell it to an authorised person or retain it to the specified extent in an account with an authorised dealer or use it for discharging a foreign exchange debt or liability to the specified extent.

The regulation further provides that the realised foreign exchange shall be deemed to be repatriated to India, when the person concerned receives in India payments in rupees from the account of a bank or an exchange house situated in any country outside India, maintained with an authorised dealer.

### **Time Limit for Surrender of Realised Foreign Exchange**

Any foreign exchange due or accrued as remuneration for services rendered, whether in or outside India, or in settlement of any lawful obligation or an income on assets held outside India or as inheritance, settlement or gift should be sold by the person concerned to an authorised person within a period of seven days of its receipt, and in all other cases within 90 days from the date of its receipt.

Regulation 6 deals with time limit for surrender of foreign exchange in certain other cases and provides that any person who has acquired or purchased foreign exchange for any purpose mentioned in the declaration made by him to an authorised person under Section 10(5) of the Act and does not use it for such purpose or for any other purpose for which purchase or acquisition of foreign exchange is permissible under the Act or the rules or regulations or direction or order made thereunder, shall surrender such foreign exchange or the unused portion thereof to an authorised person within a period of sixty days from the date of its acquisition or purchase by him.

However, in case the foreign exchange acquired or purchased by any person from an authorised person is for the purpose of foreign travel, then, the unspent balance of such foreign exchange shall be surrendered to an authorised person within ninety days from the date of return of the traveller to India, when the unspent foreign exchange is in the form of currency notes and coins; and within one hundred eighty days from the date of return of the traveller to India, when the unspent foreign exchange is in the form of travellers cheques.

**Note:** The provisions of Foreign Exchange Management (Realisation, Repatriation and Surrender of Foreign Exchange) Regulation are not applicable to foreign exchange in the form of currency of Nepal or Bhutan.

### **Exemption from Realisation or Repatriation**

Section 9 contains exemptions from the application of provisions relating to holding of foreign currency and realisation and repatriation in certain circumstances, as provided under Sections 4 and 8 of the Act respectively. Accordingly, possession of foreign currency or coins by any person or class of persons, as the Reserve Bank may specify is not prohibited. A person or class of persons may hold and operate foreign currency account within the prescribed limits as may be specified by the Reserve Bank. Foreign exchange acquired or received before 8th July, 1947, or any income arising or accruing thereon which is held outside India, in pursuance of a general or special permission of RBI, is also exempted.

Provisions relating to holding of foreign exchange, realisation and repatriation of foreign exchange are not applicable to person resident in India upto such limit as the Reserve Bank may specify, if such foreign exchange was acquired by way of gift or inheritance from certain persons mentioned above and any income

arising therefrom. Reserve Bank may also specify the exemption limit upto which the foreign exchange earned by a person from employment, business, trade, vocation services, honorarium, gifts, inheritance or other legitimate means may be possessed. Reserve Bank may also exempt such other receipts as it thinks fit.

### **POSSESSION AND RETENTION OF FOREIGN CURRENCY OR FOREIGN COINS**

Foreign Exchange Management (Possession and Retention of Foreign Currency) Regulations, 2000 provides for limits for possession and retention of foreign currency or foreign coins. Under Regulation 3 the Reserve Bank has specified following limits for possession or retention of foreign currency or foreign coins, namely:

- (i) possession without limit of foreign currency and coins by an authorised person within the scope of his authority;
- (ii) possession without limit of foreign coins by any person;
- (iii) retention by a person resident in India of foreign currency notes, bank notes and foreign currency travellers cheques not exceeding US \$ 2000 or its equivalent in aggregate, provided that such foreign exchange in the form of currency notes, bank notes and travellers cheques acquired during a visit to any place outside India by way of payment for services not arising from any business in or anything done in India; or from any person not resident in India and also who is on a visit to India, or as honorarium or gift or for services rendered or in settlement of any lawful obligation; or as a honorarium or gift while on a visit to any place outside India; or represents unspent amount of foreign exchange acquired from an authorised person for travel abroad.

Regulation 4 deals with possession of foreign exchange by a person resident in India but not permanently resident therein and provides that a person resident in India but not permanently resident therein may possess without limit foreign currency in the form of currency notes, bank notes and travellers cheques, if such foreign currency was acquired, held or owned by him when he was resident outside India and, has been brought into India in accordance with the law for the time being inforce. Explanation to regulation 4 defines the term 'not permanently resident as to mean a person resident in India for employment of a specified duration (irrespective of length thereof) or for a specific job or assignment, the duration of which does not exceed three years.

### **AUTHORISED PERSON**

Chapter III of the Act containing Sections 10-12 deals with the provisions relating to authorised person. Section 10 deals with the procedure of appointing authorised person by the Reserve Bank, Section 11 specifies the powers of the RBI to issue directions to authorised person and Section 12 prescribes the power of the RBI to inspect authorised person.

Under Section 10, any person who has made an application to the RBI may be authorised by it to act as an authorised person to deal in foreign exchange or in foreign securities as an authorised dealer, money changer or offshore banking unit or in any other manner as the RBI deem fit. This authorisation is in writing and subject to the conditions laid down by the RBI.

Normally, nationalised banks, leading non nationalized banks and foreign banks are appointed as authorized persons.

Authorised persons are required to comply with the directions of the Reserve Bank with regard to his dealing in foreign exchange or foreign security receipt with the previous permission of the Reserve Bank. However authorised person are required not to engage in any transaction involving any foreign exchange or foreign security which is not in conformity with the terms of his authorisation.

Reserve Bank of India has been empowered to revoke the authorisation granted to any person at any time in the public interest. It may also revoke the authorisation after giving an opportunity, if the authorised person

failed to comply with the conditions subject to which the authorisation was granted or contravened any of the provisions of the Act, rules, notifications or directions.

An authorised person, before undertaking any transaction on behalf of any person shall, require that person to make such declaration and give such information as will reasonably satisfy the authorised person that the transaction will not involve or is not intended to violate or contravene any provisions of the Act, rules, notification or directions. In case, the person refuses to comply with such requirements or makes only unsatisfactory compliances, the authorised person is duty bound to refuse in writing to act on behalf of such person in such transaction and report the matter to Reserve Bank.

Any person, other than an authorised person who has acquired or purchased foreign exchange for any purpose mentioned in the declaration made by him to the authorised person does not use it for such purpose, or does not surrender it to authorised person within the specified period, or uses the foreign exchange for any other purpose, which is not permitted under the provisions of the Act, such person shall be deemed to have committed contravention of the provisions of the Act.

### Power of the Reserve Bank to issue directions to authorised person

Section 11 of the Act empowers the RBI to issue directions to the authorised person in regard to making of payment or doing or desist from doing any act relating to foreign exchange or foreign security. Reserve Bank has also been empowered to issue directions to the authorised persons to furnish such information in such manner as it deems fit. If any authorised person contravenes any direction given by the RBI or fails to file the return as directed by RBI, he may be liable to a fine not exceeding Rs. 10,000/- and in the case of continuing contravention, with an additional penalty which may extend to Rs. 2,000 for every day during which such contravention continues.



*The Government of India took a policy decision to permit FDI in infrastructure companies in securities market viz stock exchanges, depositories and clearing corporation. SEBI issued a circular in this regard. RBI also issued a circular A.P.(DIR Series) Circular No. 25 dated 22.12.2006 giving certain directions to authorized dealers. The petitioner challenged the RBI Circular as invalid in as much as it restricts the trade activities of general corporate sector.*

*In Prof. Krishnaraj Goswami vs. Reserve Bank of India [(2008) 83 SCL 133 (BOM)]. Bombay High Court observed that the RBI had issued the impugned circular dated 22.12.2006 by way of directions as contemplated under section 10(4) and 11(1) of the FEMA. A bare reading of the provisions of these sections clearly shows that RBI has power to issue directions to authorized persons and this power is wide enough to cover any kind of directions so far it provides for regulation of foreign exchange management. The contention of petitioner, that RBI had no jurisdiction to issue such circulars, can not be accepted. Section 10(4) clearly stipulates that an authorized person, in all dealings, is bound by the directions, general, or special, issued by RBI. Similarly, section 11(1) provides that RBI may, for the purpose of securing compliance of the provisions of the FEMA and of any rules, regulations and directions made thereunder, give to the authorized persons any direction in regard to making of payment or the doing or desist from doing of any act relating to foreign exchange or foreign security.*

*The petitioner had not challenged the policy decision of the Central Government, but had merely questioned the incidental act i.e. the impugned circular. In any event, these are policy decisions which fall within the domain of the authorities concerned in the Central Government. The effect and repercussions of such policy decision can hardly be subject matter of judicial review. Policy decision unless and until are reversed or inconsistent with the constitutional mandate or a patent abuse of power, judicial intervention will normally be not necessitated. Petition dismissed.*

### Power of Reserve Bank to Inspect authorised person

Section 12 of the Act empowers RBI to inspect the business of any authorised person for the purpose of verifying the correctness of any statement/information or particulars furnished. In case authorised person fails to furnish the information sought, the RBI can initiate inspection of the authorised person for obtaining such information. RBI may also inspect the business of an authorised person for securing compliance with the provisions of the Foreign Exchange Management Act or any of the Rules, Regulations or directions. The Reserve Bank may make an order in writing authorising any of its officer for this purpose.

When an inspection is initiated by the Reserve Bank, it shall be the duty of every authorised person (where the authorised person is a company or firm, every director partner or officer of such a company or firm), to produce before the inspecting officer, such books, accounts and other documents in his custody and to furnish any statement or information relating to the affairs of such authorised person within the time limit and the manner in which such inspecting officer may direct.

#### ***Who is an Authorized Dealer?***

An Authorised Dealer is any person specifically authorized by the Reserve Bank under Section 10(1) of FEMA, 1999, to deal in foreign exchange or foreign securities.



### CONTRAVICTION AND PENALTIES

Chapter IV of the Act containing Sections 13 to 15 deals with contravention and penalties. Section 13 deals with penalties, Section 14 provides for enforcement of the orders of Adjudicating Authority and Section 15 deals with compounding of contraventions.

Section 13 provides that any person contravening any provision of the Act, or any condition subject to which the authorisation is granted by the RBI, shall be liable for penalty upon adjudication, which may extend upto thrice the sum involved in such contravention where such amount is quantifiable or upto two lakh rupees where the amount is not quantifiable. If the contravention continues, the penalty of Rs. 5,000 per day during the period in which the contravention continues, shall be imposed.

In addition to the powers to impose penalty, the Adjudicating Authority, adjudging any contravention is empowered to confiscate to the Government of India any currency, security or any other money or property in respect of which the contravention has taken place and may further direct that the foreign exchange holdings if any, of the persons committing the contravention shall be brought back either to India or retained outside India, in accordance with the directions.

#### **Enforcement of the Orders of Adjudicating Authority**

In terms of Section 14 of the Act, if any person fails to make full payment of the penalty imposed within a period of ninety days from the date on which the notice of payment of such penalty is served on him, he shall be liable for civil imprisonment. However, no order of arrest and detention in civil imprisonment should be made unless the Adjudicating Authority issue showcause notice to defaulter as to why he should not be committed to civil imprisonment and unless the Adjudicating Authority, for reasons in writing, is satisfied that the defaulter has transferred, concealed or removed any part of his property or he has refused to pay the penalty despite the fact he had means to pay the arrears.

The defaulter may be issued by the Adjudicating Authority a warrant of arrest, on its satisfaction by affidavit or otherwise, that the defaulter is likely to abscond or leave the local limit of its jurisdiction. A warrant issued

by one Adjudicating Authority may also be executed by any other Adjudicating Authority within whose jurisdiction the defaulter is found, and the person so arrested shall be brought before the Adjudicating Authority issuing warrant within 24 hours of arrest, excluding however the time taken in journey.

On arrest, if the defaulter pays the amount entered in the warrant as due and the cost of arrest to the arresting officer, such officer is under obligation to release him at once.

The Act gives an opportunity to make an appeal to Appellate Tribunal within forty five days from the date on which a copy of the order made by the Adjudicating Authority or the Special Director (Appeals) is received by the aggrieved person. This period of forty-five days for filing the appeal may be relaxed by the Appellate Tribunal if it is satisfied that there was sufficient cause for not filing the appeal in time.

### Compounding of Contraventions

#### ***What is meant by contravention and compounding of contravention?***

*Contravention is a breach of the provisions of the Foreign Exchange Management Act (FEMA), 1999 and rules/ regulations/ notification/ orders/ directions/ circulars issued there under.*



*Compounding refers to the process of voluntarily admitting the contravention, pleading guilty and seeking redressal. The Reserve Bank is empowered to compound any contraventions as defined under section 13 of FEMA, 1999 except the contravention under section 3(a) for a specified sum after offering an opportunity of personal hearing to the contravener. It is a voluntary process in which an individual or a corporate seeks compounding of an admitted contravention. It provides comfort to any person who contravenes any provisions of FEMA, 1999 [except section 3(a) of the Act] by minimizing transaction costs.*

*Willful, malafide and fraudulent transactions are, however, viewed seriously, which will not be compounded by the Reserve Bank.*

Section 15 empowers the Directorate of Enforcement or Officers of the Directorate of Enforcement and of the Reserve Bank to compound the offences. This section provides that contravention under Section 13 may be compounded within 180 days from the date of receipt of application. Sub-section (2) provides that where the contravention has been compounded, the accused person is relieved from further proceedings for the contravention.

Foreign Exchange (Compounding Proceedings) Rules, 2000 deals with procedure for compounding of contravention of the provisions of the Act. Rule 3 defines the Compounding Authority as to mean the persons authorised by the Central Government under Sub-section (1) of Section 15 of the Act namely:

- (a) an officer of the Enforcement Directorate not below the rank of Deputy Director or Deputy Legal Advisor (DLA).
- (b) an officer of the Reserve Bank of India not below the rank of the Assistant General Manager.

### **Powers of Reserve Bank to Compound Contravention**

Rule 4 empowers the RBI to compound only quantifiable contravention committed by any person of the provisions of Section 7 or Section 8 or Section 9, or Third Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000 in the following manner:

- (a) where the sum involved in such contravention is ten lakhs rupees or below, by the Assistant General Manager of the Reserve Bank of India;

- (b) where the sum involved in such contravention is more than rupees ten lakhs but less than rupees forty lakhs by the Deputy General Manager of Reserve Bank of India;
- (c) where the sum involved in the contravention is rupees forty lakhs or more but less than rupees one hundred lakhs by the General Manager of Reserve Bank of India; and
- (d) the sum involved in such contravention is rupees one hundred lakhs or more, by the Chief General Manager of the Reserve Bank of India.

### **Powers of Enforcement Directorate to Compound Contravention**

Rule 5 specifies the cases in which only quantifiable contraventions of the provisions of the Act [other than Section 7 or Section 8 or Section 9 or Third Schedule to the Foreign Exchange (Current Account Transactions) Rules, 2000] can be compounded by the Enforcement Directorate. These include:

- (a) where the sum involved in such contravention is five lakhs rupees or below, by the Deputy Director of the Directorate of Enforcement;
- (b) where the sum involved in such contravention is more than rupees five lakhs but less than rupees ten lakhs by the Additional Director of the Directorate of Enforcement;
- (c) where the sum involved in the contravention is rupees ten lakhs or more but less than rupees fifty lakhs by the Special Director of the Directorate of Enforcement;
- (d) where the sum involved in the contravention is rupees fifty lakhs or more, but less than rupees one crore by Special Director with Deputy Legal Advisor of the Directorate of Enforcement;
- (e) where the sum involved in such contravention is one crore rupees or more, by the Director of Enforcement with Special Director of the Enforcement Directorate.

The benefit of above provisions shall not be available in case a contravention committed by any person within a period of three years from the date on which a similar contravention committed by him was compounded under these rules. However, any second or subsequent contravention committed after the expiry of a period of three years from the date on which the contravention was previously compounded shall be deemed to be a first contravention.

Where any contravention is compounded before the adjudication of any contravention under Section 16, no inquiry shall be held for adjudication of such contravention in relation to such contravention against the person in relation to whom the contravention is so compounded. In case the compounding of any contravention is made after making of a complaint under Sub-section (3) of Section 16, such compounding shall be brought by the authority specified in Rule 4 or Rule 5 in writing, to the notice of the Adjudicating Authority and on such notice of the compounding of the contravention being given, the person in relation to whom the contravention is so compounded shall be discharged.

### **Payment of Compounded Amount**

Rule 9 deals with payment of amount compounded. Where a contravention has been compounded in terms of Rule 8(2) the sum involved in such contravention shall be deposited within fifteen days from the date of the order of compounding of such contravention by demand draft in favour of the Compounding Authority. In case a person fails to pay the sum compounded within the specified time, he shall be deemed to have never made an application for compounding of any contravention and the provisions of the Act for contravention shall apply to him.

However, no contravention shall be compounded if an appeal has been filed with the Special Director (Appeals) under Section 17 or with Appellate Tribunal under Section 19. Every order of compounding the contravention shall specify the provisions of the Act or the rules, directions, requisitions or orders made

thereunder in respect of which contravention has taken place alongwith details of the alleged contravention and a copy thereof shall be supplied to the applicant and the Adjudicating Authority as the case may be.

## **ADJUDICATION AND APPEAL**

Chapter V containing Sections 16-35 deal with the adjudication and appeal.

### **Appointment of Adjudicating Authority**

Section 16 empowers the Central Government to appoint by notification in the Official Gazette as many Adjudicating Authorities as it may think fit for holding enquiries under Section 13. The Central Government is, however under obligation to specify the jurisdiction of the Adjudicating Authority. The Adjudicating Authority has been empowered to hold any enquiry on a complaint made in writing by an officer authorised by a general or special order by the Central Government.

In case, a complaint has been made in respect of a person alleged to have committed the contravention, such person shall be given a reasonable opportunity of being heard before imposing any penalty under Section 13. The Adjudicating Authority has discretion to demand from the persons against whom a complaint is made a bond or guarantee for any such amount as he thinks fit, if he is of the opinion that such persons likely to abscond or evade the payment of penalty, if imposed.

### **Appeal to Special Director (Appeals)**

Section 17 of the Act provides for appointment of one or more Special Directors (Appeals) to hear appeals against the orders of the Adjudicating Authorities. In this context, the Central Government has been empowered to appoint by notification Special Directors (Appeals) specifying their jurisdiction over matters and places.

An appeal to the Special Director (Appeals) may be made against the orders of the Assistant Director or Deputy Director of enforcement, acting as Adjudicating Authority. The appeal against the order of Adjudicating Authority shall be made in the prescribed form along with requisite fee, within forty five days from the date of the receipt of the order by aggrieved person. The Special Director (Appeals) has however, been empowered to entertain appeal after the expiry of the said period of forty five days.

### **Establishment of Appellate Tribunal**

Under Section 18, the Central Government is empowered to establish an Appellate Tribunal, by a notification in the Official Gazette, to hear appeals against the orders of Adjudication Authorities and Special Director (Appeals). The Central Government or any person aggrieved by the orders of Adjudicating Authority or Special Director (Appeals) may prefer an appeal to the Appellate Tribunal under Section 19 of the Act.

Section 20 of the Act empowers the Central Government to appoint a Chairperson and as many members as it may deem fit to the Appellate Tribunal. The jurisdiction of the Appellate Tribunal may be exercised by benches. A bench may be constituted by the Chairperson with one or more member as the Chairperson deem fit. The Chairperson can also transfer member of one bench to another bench. The Appellate Tribunal shall sit ordinarily at New Delhi for hearing. The Central Government however may, in consultation with the Chairperson, notify the sitting of the Tribunal elsewhere as it may deem fit.

A person who is or has been or is qualified to be a judge of a High Court shall be eligible for the appointment as chairperson of Appellate Tribunal. A person who is or has been or is eligible to be a district judge shall be eligible for appointment as a member of Appellate Tribunal. A member of the Indian Legal Service and holding the post in Grade I of that Services or the member of Indian Revenue Service and holding the post equivalent to a Joint Secretary to the Government of India, shall be eligible to be appointed as Special Director (Appeals).

The Chairperson and Members will hold office for a period of 5 years from the date of assuming office. However, no chairperson or member shall hold office on attaining the age of 65 years and 62 years respectively.

### **Appeal to High Court**

A right to appeal to High Court lies with the appellant who is aggrieved by the decision of the Tribunal. Such appeal must be filed within 60 days from the date of communication of the decision or order of the Tribunal. The appeal to the High Court can be made on any question of law arising out of such order. A relaxation for a maximum period of sixty days for making an appeal may be granted by the High Court, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the specified period.

### **Directorate of Enforcement**

Section 36 of the Act empowers the Central Government to establish a Directorate of Enforcement with a Director and other officers or class of Officers, for the purposes of the enforcement of the Act. The Central Government has also been empowered to authorise Director, Additional Director, Special Director or Deputy Director to appoint officers of enforcement below the rank of Assistant Director of Enforcement to exercise the powers and discharge the duties conferred or imposed on him under the Act.

The Central Government, may by order and with prescribed conditions and limitations, authorise any officers of customs or Central Excise or any police officer or officers of Central or State Government to exercise such powers and discharge such duties of the Director of Enforcement or any other officer of the Enforcement as stated in the order.

### **Investigation**

Section 37 of the Act empowers the Director of Enforcement and other officers below the rank of an Assistant Director to take up for investigation the contravention referred to in Section 13 of the Act. In addition, the Central Government may also authorise any officer or class of officers in the Central Government, State Government, Reserve Bank of India, not below the rank of Under Secretary to Government of India, to investigate any contravention under Section 13 of the Act. The officers so appointed shall exercise the like powers which are conferred on income tax authorities under the Income Tax Act, 1961, subject to such conditions and limitations as laid down under that Act.

In this context, Foreign Exchange Management (Encashment of Draft, Cheque Instrument and Payment of Interest) Rules, 2000 provides that where investigation referred to in Section 37 of the Act is being taken up into any alleged contravention of any provisions of the Act or rule, regulation, direction or order or violation of any condition subject to which Reserve Bank of India gives authorisation, and any draft, cheque or other instrument relevant for such investigation, such officer shall send such draft, cheque or other instrument to the Reserve Bank of India or to an authorised person as the officer may specify for encashment. The Reserve Bank of India or the authorised person is required to take steps without delay for encashment of the draft, cheque or other instrument and to credit the proceeds of such encashment (less any commission and expenses incurred for such encashment) to a separate account in the name of the Directorate of Enforcement.

The Central Government is required to indemnify the Reserve Bank of India or an authorised person against any liability which may incur by reason of or in connection with the encashment of the draft, cheque or other instrument delivered to it.

### **Contravention by Companies**

Section 42 of the Act deals with contravention of the provisions of the Act by the Companies and provides that where the person committing the contravention of the Act or Rules happened to be a company, every

person who at the time the contravention was committed, was in charge of and was responsible to the company for the conduct of the business of the company shall be deemed to be guilty of the contravention and liable to be proceeded against and punished accordingly. However, no such persons shall be deemed to be guilty of committing any offence if he proves that such contravention took place without his knowledge or that he exercised adequate steps to prevent such contravention.

In case the contravention is committed by a company and it is proved that such contravention is committed with the knowledge, consent and connivance or is attributed to the neglect on the part of any director, manager or secretary or other officer of the company, they will also be deemed to be guilty of contravention and liable to be proceeded against and punished accordingly.

### **LESSON ROUND UP**

- The Foreign Exchange Management Act has repealed the FERA.
- The Foreign Exchange Management Act, 1999 is an Act to facilitate external trade and payments and for promoting the orderly development and maintenance of foreign exchange market in India.
- Foreign exchange means 'foreign currency' and includes:- (i) deposits, credits and balances payable in any foreign currency; (ii) drafts, travellers' cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency; and (iii) drafts, travellers' cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency.
- Capital Account transactions means any transaction which alters the assets or liabilities including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of person resident outside India and includes the transactions specified in Sub-section (3) of Section 6 of the Act.
- Current Account Transaction means a transaction other than a capital account transaction and includes payments due in connection with foreign trade, other current business, services and short term banking and credit facilities in the ordinary course of business; payments due as interest on loan and as net income from investments; remittances for living expenses of parents, spouse and children residing abroad and expenses in connection with foreign travel, education and medical care of parents, spouse and children.
- Foreign Direct Investment (FDI) is a category of cross border investment made by a resident in one economy (the direct investor) with the objective of establishing a 'lasting interest' in an enterprise (the direct investment enterprise) i.e. resident in an economy other than that of the direct investor.
- Joint Ventures/Wholly Owned Subsidiaries abroad promote economic co-operation between India and the host countries. They result in transfer of technology and skills, sharing the results of Research & Development, access to the global market, promotion of the brand image, generation of employment and utilization raw materials available in India and the host country, increased exports of plant and machinery and goods and services from India, foreign exchange earnings through dividend earnings, royalty, technical know-how fee, etc.
- Resident outside India and permitted by the Reserve Bank to establish a branch or a liaison office in India may undertake or carry on any specified activity.
- Compounding refers to the process of voluntarily admitting the contravention, pleading guilty and seeking redressal. The Reserve Bank is empowered to compound any contraventions as defined under section 13 of FEMA, 1999 except the contravention under section 3(a) for a specified sum after offering an opportunity of personal hearing to the contravener. It is a voluntary process in which an individual or a corporate seeks compounding of an admitted contravention. It provides comfort to any person who contravenes any provisions of FEMA, 1999 [except section 3(a) of the Act] by minimizing transaction costs.

## SELF TEST QUESTIONS

1. Define the Capital Account Transactions and enumerate permissible capital account transactions in relation to persons resident in India and resident outside India?
  2. Discuss the Acquisition and Transfer of Immovable Property in India under FEMA?
  3. Discuss the establishment of branch or office or place of business in India under FEMA.
  4. Define Authorised person? Briefly discuss the powers of RBI to give directions to Authorised persons?
  5. Write short note on the following:
    - (i) Compounding of Contraventions
    - (ii) Directorate of Enforcement
    - (iii) Appellate Tribunal
    - (iv) Investigation
    - (v) Export of Goods and Services.

# FOREIGN EXCHANGE MANAGEMENT [FOREIGN CONTRIBUTION (REGULATION) ACT, 2010]

## Section II

### LESSON OUTLINE

- Objective of FCRA
- Foreign contribution
- Foreign Source
- Foreign hospitality
- Regulation of foreign contribution and foreign hospitality
- Certificate of Registration
- Application for Renewal
- Renewal of Certificate
- Cancellation of Certificate
- Management of Foreign Contribution
- Intimation to Government
- Obligation of Banks under FCRA
- Inspection
- Audit
- Confiscation
- Adjudication
- Offences and penalties
- Appeal
- Compounding of offences

### LEARNING OBJECTIVES

Foreign Contribution (Regulation) Act, 2010 is internal security legislation and regulated by Ministry of Home Affairs which prohibits certain classes of persons from receiving 'foreign contribution'. It also restricts certain classes of persons from accepting foreign hospitality while visiting any country or territory outside India, without the prior permission of the Central Government. The Act provides that persons having definite cultural, economic, educational, religious and social programmes should get themselves registered with the Government of India before accepting any 'foreign contribution'. "Foreign contribution" means the donation, delivery or transfer made by any foreign source of any article, not being an article given to a person as a gift for his personal use, if the market value, in India, of such article, on the date of such gift, is not more than such sum as may be specified from time to time, by the Central Government by the rules made by it in this behalf; of any currency, whether Indian or foreign; any security as defined under Securities Contracts (Regulation) Act, 1956 and the Foreign Exchange Management Act, 1999.

The Act mandates that every bank or authorized person in foreign exchange shall report to specified authority, the prescribed amount of foreign remittance, source and manner in which foreign remittance was received and other particulars in such form and manner as may be prescribed. The object of the study is to familiarize the students with the legal requirements stipulated under the FCRA, 2010.

The object of the Foreign Contribution (Regulation) Act, 2010 is to regulate the acceptance and utilisation of foreign contribution or foreign hospitality by certain individuals or associations or companies and to prohibit acceptance and utilisation of foreign contribution or foreign hospitality for any activities detrimental to the national interest and for matters connected therewith or incidental thereto.

## INTRODUCTION

The Foreign Contribution (Regulation) Act, 1976 was enacted to regulate the acceptance and utilization of foreign contribution or hospitality with a view to ensuring that the Parliamentary institutions, political associations, academic and other voluntary organizations as well as individuals working in important areas of national life may function in a manner consistent with the values of sovereign democratic republic. The Act was amended in 1984 to extend its provisions to cover second and subsequent recipients of foreign contribution and to the members of higher judiciary, besides introducing the system of grant of registration to the association receiving foreign contribution.

Significant developments have taken place since 1984 such as change in internal security scenario, an increased influence of voluntary organizations, spread of use of communication and information technology, quantum jump in the amount of foreign contribution being received, and large scale growth in the number of registered organizations. This has necessitated large scale changes in the Act of 1976 and therefore, it was thought appropriate to replace the FCRA, 1976 by a new legislation to regulate the acceptance and utilization of foreign contribution and foreign hospitality by a person or association.

The Foreign Contribution (Regulation) Act, 2010 has come into effect from May 1, 2011. The Ministry of Home Affairs has issued the necessary Gazette Notification vide S.O. 999 (E) dated the 29th April, 2011 in this regard. The Ministry of Home Affairs has also issued a Gazette Notification vide G.S.R. 349 (E) dated the 29th April, 2011 notifying the Foreign Contribution (Regulation) Rules, 2011 made under section 48 of FCRA, 2010. The FCR Rules, 2011 have come into force simultaneously with FCRA, 2010.

## DEFINITIONS

The definitions of the following terms used in the statute are relevant for understanding the operative provisions of the Foreign Contribution (Regulation) Act, 2010.

**“Association”** means an association of individuals, whether incorporated or not, having an office in India and includes a society, whether registered under the Societies Registration Act, 1860, or not, and any other organisation, by whatever name called [Section 2(1)(a)]

**“Authorised person in foreign exchange”** means an authorised person referred to in clause (c) of section 2 of the Foreign Exchange Management Act, 1999 [Section 2(1)(b)]

**“Bank”** means a banking company as referred to in clause (c) of section 5 of the Banking Regulation Act, 1949 [Section 2(1)(c)]

**“Candidate for election”** means a person who has been duly nominated as a candidate for election to any Legislature [Section 2(1)(d)]

**“Certificate”** means certificate of registration granted under sub-section (3) of section 12 [Section 2(1)(e)]

**“Company”** shall have the meaning assigned to it under clause (17) of section 2 of the Income-tax Act, 1961 Section 2(1)(f);

**“Foreign company”** means any company or association or body of individuals incorporated outside India and includes—

- (i) a foreign company within the meaning of section 591 of the Companies Act, 1956 (1 of 1956);

- (ii) a company which is a subsidiary of a foreign company;
- (iii) the registered office or principal place of business of a foreign company referred to in sub clause (i) or company referred to in sub-clause (ii);
- (iv) a multi-national corporation.

*Explanation.*— For the purposes of this sub-clause, a corporation incorporated in a foreign country or territory shall be deemed to be a multi-national corporation if such corporation,—

- (a) has a subsidiary or a branch or a place of business in two or more countries or territories; or
- (b) carries on business, or otherwise operates, in two or more countries or territories; [Section 2(1)(g)]

**“Foreign contribution”** means the donation, delivery or transfer made by any foreign source,—

- (i) of any article, not being an article given to a person as a gift for his personal use, if the market value, in India, of such article, on the date of such gift, is not more than such sum as may be specified from time to time, by the Central Government by the rules made by it in this behalf;
- (ii) of any currency, whether Indian or foreign;
- (iii) of any security as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 and includes any foreign security as defined in clause (o) of section 2 of the Foreign Exchange Management Act, 1999.

*Explanation 1.*— A donation, delivery or transfer of any article, currency or foreign security referred to in this clause by any person who has received it from any foreign source, either directly or through one or more persons, shall also be deemed to be foreign contribution within the meaning of this clause.

*Explanation 2.*— The interest accrued on the foreign contribution deposited in any bank referred to in sub-section (1) of section 17 or any other income derived from the foreign contribution or interest thereon shall also be deemed to be foreign contribution within the meaning of this clause.

*Explanation 3.*— Any amount received, by any person from any foreign source in India, by way of fee (including fees charged by an educational institution in India from foreign student) or towards cost in lieu of goods or services rendered by such person in the ordinary course of his business, trade or commerce whether within India or outside India or any contribution received from an agent of a foreign source towards such fee or cost shall be excluded from the definition of foreign contribution within the meaning of this clause [Section 2(1)(h)].

**“Foreign hospitality”** means any offer, not being a purely casual one, made in cash or kind by a foreign source for providing a person with the costs of travel to any foreign country or territory or with free boarding, lodging, transport or medical treatment [Section 2(1)(i)].

**“Foreign source”** includes,—

- (i) the Government of any foreign country or territory and any agency of such Government;
- (ii) any international agency, not being the United Nations or any of its specialised agencies, the World Bank, International Monetary Fund or such other agency as the Central Government may, by notification, specify in this behalf;
- (iii) a foreign company;
- (iv) a corporation, not being a foreign company, incorporated in a foreign country or territory;

- (v) a multi-national corporation referred to in sub-clause (iv) of clause (g);
- (vi) a company within the meaning of the Companies Act, 1956 and more than one-half of the nominal value of its share capital is held, either singly or in the aggregate, by one or more of the following, namely:—
  - (A) the Government of a foreign country or territory;
  - (B) the citizens of a foreign country or territory;
  - (C) corporations incorporated in a foreign country or territory;
  - (D) trusts, societies or other associations of individuals (whether incorporated or not), formed or registered in a foreign country or territory;
  - (E) foreign company;
- (vii) a trade union in any foreign country or territory, whether or not registered in such foreign country or territory;
- (viii) a foreign trust or a foreign foundation, by whatever name called, or such trust or foundation mainly financed by a foreign country or territory;
- (ix) a society, club or other association of individuals formed or registered outside India;
- (x) a citizen of a foreign country[ Section 2(1)(j)]

**“Legislature”** means —

- (A) either House of Parliament;
- (B) the Legislative Assembly of a State, or in the case of a State having a Legislative Council, either House of the Legislature of that State;
- (C) Legislative Assembly of a Union territory constituted under the Government of Union Territories Act, 1963;
- (D) Legislative Assembly for the National Capital Territory of Delhi referred to in the Government of National Capital Territory of Delhi Act, 1991;
- (E) Municipality as defined in clause (e) of article 243P of the Constitution;
- (F) District Councils and Regional Councils in the States of Assam, Meghalaya, Tripura and Mizoram as provided in the Sixth Schedule to the Constitution[ Section 2(1)(k)]

**“Person”** includes—

- (i) an individual;
- (ii) a Hindu undivided family;
- (iii) an association;
- (iv) a company registered under section 25 of the Companies Act, 1956 [Section 2(1)(m)]

**“Political party”** means—

- (i) an association or body of individual citizens of India—
  - (A) to be registered with the Election Commission of India as a political party under section 29A of the Representation of the People Act, 1951; or

- (B) which has set up candidates for election to any Legislature, but is not so registered or deemed to be registered under the Election Symbols (Reservation and Allotment) Order, 1968;
- (ii) a political party mentioned in column 2 of Table 1 and Table 2 to the notification of the Election Commission of India No.56/J&K/02, dated the 8th August, 2002, as in force for the time being [Section 2(1)(n)]

It may be noted that Words and expressions used herein and not defined in this Act but defined in the Representation of the People Act, 1950 or the Representation of the People Act, 1951 or the Foreign Exchange Management Act, 1999 shall have the meanings respectively assigned to them in those Acts.

## **REGULATION OF FOREIGN CONTRIBUTION AND FOREIGN HOSPITALITY**

### **Prohibition to accept foreign contribution**

Section 3(1) of the Act, imposes restriction on acceptance of foreign contribution by candidate for election; correspondent, columnist, cartoonist, editor, owner, printer or publisher of a registered newspaper; Judge, Government servant or employee of any corporation or any other body controlled or owned by the Government; member of any Legislature; political party or office-bearer thereof; organisation of a political nature as may be specified by the Central Government; association or company engaged in the production or broadcast of audio news or audio visual news or current affairs programmes through any electronic mode, or any other electronic form as defined in clause (r) of sub-section (1) of section 2 of the Information Technology Act, 2000 or any other mode of mass communication; correspondent or columnist, cartoonist, editor, owner of the association or company. A “corporation” for the above purpose means a corporation owned or controlled by the Government and includes a Government company as defined in section 617 of the Companies Act, 1956.

Sub-section (2)(a) of Section 3 provides that no person, resident in India, and no citizen of India resident outside India, shall accept any foreign contribution, or acquire or agree to acquire any currency from a foreign source, on behalf of any political party, or any person, prohibited from accepting any foreign contribution.

Sub-section (2) (b) mandates that no person, resident in India, shall deliver any currency, whether Indian or foreign, which has been accepted from any foreign source, to any person if he knows or has reasonable cause to believe that such other person intends, or is likely, to deliver such currency to any political party or any person, prohibited from accepting any foreign contribution.

Section 3(2)(c) provides that no citizen of India resident outside India shall deliver any currency, whether Indian or foreign, which has been accepted from any foreign source, to any political party or any person specified in sub-section (1) of section 3 , or both or any other person, if he knows or has reasonable cause to believe that such other person intends, or is likely, to deliver such currency to a political party or to any person specified in sub-section (1) of section 3, or both.

Section 3(3) provides that no person receiving any currency, whether Indian or foreign, from a foreign source on behalf of any person or class of persons, referred to in section 9, shall deliver such currency to any person other than a person for which it was received, or to any other person, if he knows or has reasonable cause to believe that such other person intends, or is likely, to deliver such currency to a person other than the person for which such currency was received.

### **Person to whom section 3 does not apply**

Section 4 provides that nothing contained in section 3 shall apply to the acceptance, by any person specified

in that section, of any foreign contribution where such contribution is accepted by him, subject to the provisions of section 10,—

- (a) by way of salary, wages or other remuneration due to him or to any group of persons working under him, from any foreign source or by way of payment in the ordinary course of business transacted in India by such foreign source; or
- (b) by way of payment, in the course of international trade or commerce, or in the ordinary course of business transacted by him outside India; or
- (c) as an agent of a foreign source in relation to any transaction made by such foreign source with the Central Government or State Government; or
- (d) by way of a gift or presentation made to him as a member of any Indian delegation, provided that such gift or present was accepted in accordance with the rules made by the Central Government with regard to the acceptance or retention of such gift or presentation; or
- (e) from his relative; or
- (f) by way of remittance received, in the ordinary course of business through any official channel, post office, or any authorised person in foreign exchange under the Foreign Exchange Management Act, 1999; or
- (g) by way of any scholarship, stipend or any payment of like nature:

Further in case any foreign contribution received by any person specified under section 3, for any of the purposes other than those specified under this section, such contribution shall be deemed to have been accepted in contravention of the provisions of section 3.

#### **Procedure to notify an organization of a political nature**

Section 5(1) provides that the Central Government may, having regard to the activities of the organisation or the ideology propagated by the organisation or the programme of the organisation or the association of the organisations with the activities of any political party, by an order published in the Official Gazette, specify such organisation as an organisation of a political nature not being a political party, referred to in clause (f) of sub-section (1) of section 3. Further, the Central Government may, frame the guidelines specifying the ground or grounds on which an organisation shall be specified as an organisation of a political nature.

#### **Restriction on acceptance of foreign hospitality**

Section 6 prohibits acceptance of foreign hospitality by certain persons except with the prior permission of Central Government. Accordingly no member of a Legislature or office-bearer of a political party or Judge or Government servant or employee of any corporation or any other body owned or controlled by the Government shall, while visiting any country or territory outside India, accept, except with the prior permission of the Central Government, any foreign hospitality.

However, it shall not be necessary to obtain any such permission for an emergent medical aid needed on account of sudden illness contracted during a visit outside India, but, where such foreign hospitality has been received, the person receiving such hospitality shall give, within one month from the date of receipt of such hospitality an intimation to the Central Government as to the receipt of such hospitality, and the source from which, and the manner in which, such hospitality was received by him.

### Prohibition to transfer foreign contribution to other person

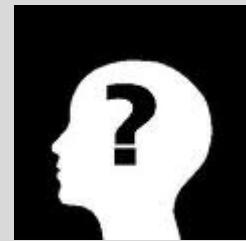
Section 7 prohibits the transfer of foreign contribution to other person. Accordingly, no person who is registered and granted a certificate or has obtained prior permission under the Act; and receives any foreign contribution, shall transfer such foreign contribution to any other person unless such other person is also registered and had been granted the certificate or obtained the prior permission under the Act.

However, such person may transfer, with the prior approval of the Central Government, a part of such foreign contribution to any other person who has not been granted a certificate or obtained permission under the Act in accordance with the rules made by the Central Government.

### ***Which are the organisations/individuals specifically debarred from receiving foreign contribution?***

*The following are the persons prohibited from accepting foreign contribution:*

- (a) Candidate for election;
- (b) Correspondent, columnist, cartoonist, editor, owner, printer or publisher of a registered newspaper;
- (c) Judge, government servant or employee of any entity controlled or owned by the Government;
- (d) Member of any Legislature;
- (e) Political party or office bearers thereof;
- (f) Organisations of a political nature as may be specified;
- (g) Associations or companies engaged in the production or broadcast of audio news or audiovisual news or current affairs programmes through any electronic mode or form or any other mode of mass communication;
- (h) Correspondent or columnist, cartoonist, editor, owner of the association or company referred to in (g) above.



### Utilization of foreign contribution

Section 8 (1)(a) provides that every person, who is registered and granted a certificate or given prior permission under the Act and receives any foreign contribution, shall utilise such contribution for the purposes for which the contribution has been received. Further any foreign contribution or any income arising out of it shall not be used for speculative business and that the Central Government shall, by rules, specify the activities or business which shall be construed as speculative business for the purpose of this section.

Section 8 (1) (b) provides that every person, who is registered and granted a certificate or given prior permission under this Act and receives any foreign contribution, shall not defray as far as possible such sum, not exceeding fifty per cent of such contribution, received in a financial year, to meet administrative expenses. Further administrative expenses exceeding fifty per cent of such contribution may be defrayed with prior approval of the Central Government.

The Central Government prescribes the elements which shall be included in the administrative expenses and the manner in which the administrative expenses shall be calculated.

### Power of Central Government to prohibit receipt of foreign contribution

Section 9 deals with power of Central Government to prohibit receipt of foreign contribution, etc., in certain cases. Accordingly, the Central Government has been empowered to -

- (a) prohibit any person or organisation not specified in section 3, from accepting any foreign contribution;
- (b) require any person or class of persons, not specified in section 6, to obtain prior permission of the Central Government before accepting any foreign hospitality;
- (c) require any person or class of persons not specified in section 11, to furnish intimation within such time and in such manner as may be prescribed as to the amount of any foreign contribution received by such person or class of persons as the case may be, and the source from which and the manner in which such contribution was received and the purpose for which and the manner in which such foreign contribution was utilised;
- (d) without prejudice to the provisions of sub-section (1) of section 11, require any person or class of persons specified in that sub-section to obtain prior permission of the Central Government before accepting any foreign contribution;
- (e) require any person or class of persons, not specified in section 6, to furnish intimation, within such time and in such manner as may be prescribed, as to the receipt of any foreign hospitality, the source from which and the manner in which such hospitality was received.

However, no such prohibition or requirement shall be made unless the Central Government is satisfied that the acceptance of foreign contribution by such person or class of persons, as the case may be, or the acceptance of foreign hospitality by such person, is likely to affect prejudicially the sovereignty and integrity of India; or public interest; or freedom or fairness of election to any Legislature; or friendly relations with any foreign State; or harmony between religious, racial, social, linguistic or regional groups, castes or communities.

### Power to prohibit payment of currency received in contravention of the Act

Section 10 provides that where the Central Government is satisfied, after making such inquiry as it may deem fit, that any person has in his custody or control any article or currency or security, whether Indian or foreign, which has been accepted by such person in contravention of any of the provisions of this Act, it may, by order in writing, prohibit such person from paying, delivering, transferring or otherwise dealing with, in any manner whatsoever, such article or currency or security save in accordance with the written orders of the Central Government and a copy of such order shall be served upon the person so prohibited in the prescribed manner.

#### Who can receive foreign contribution?

*An association having a definite cultural, economic, educational, religious or social programme shall accept foreign contribution unless such person obtains a certificate of registration / prior permission from the Central Government.*



### Registration of certain persons with Central Government

Section 11(1) requires that person having a definite cultural, economic, educational, religious or social

programme shall accept foreign contribution if such person obtains a certificate of registration from the Central Government.

It may be noted that any association registered with the Central Government under section 6 or granted prior permission under that section of the Foreign Contribution (Regulation) Act, 1976, as it stood immediately before the commencement of this Act, shall be deemed to have been registered or granted prior permission, as the case may be, under this Act and such registration shall be valid for a period of five years from the date on which this section comes into force.

Sub-section (2) of Section 11 provides that every person referred to in sub-section (1) may, if it is not registered with the Central Government under that sub-section, accept any foreign contribution only after obtaining the prior permission of the Central Government and such prior permission shall be valid for the specific purpose for which it is obtained and from the specific source. Further if the person referred to in sub-sections (1) and (2) has been found guilty of violation of any of the provisions of this Act or the Foreign Contribution (Regulation) Act, 1976, the unutilised or unreceived amount of foreign contribution shall not be utilised or received, as the case may be, without the prior approval of the Central Government.

Sub-section (3) of Section 11 provides that the Central Government may, by notification in the Official Gazette, specify the person or class of persons who shall obtain its prior permission before accepting the foreign contribution; or the area or areas in which the foreign contribution shall be accepted and utilised with the prior permission of the Central Government; or the purpose or purposes for which the foreign contribution shall be utilised with the prior permission of the Central Government; or the source or sources from which the foreign contribution shall be accepted with the prior permission of the Central Government.

### **Grant of certificate of registration**

Section 12(1) provides that an application by a person for grant of certificate or giving prior permission, shall be made to the Central Government in such form and manner and alongwith such fee, as may be prescribed. On receipt of an application, the Central Government shall, by an order, if the application is not in the prescribed form or does not contain any of the particulars specified in that form, reject the application. If on receipt of an application for grant of certificate or giving prior permission and after making such inquiry as the Central Government deems fit, it is of the opinion that the conditions specified in sub-section (4) are satisfied, it may, ordinarily within ninety days from the date of receipt of application, register such person and grant him a certificate or give him prior permission, as the case may be, subject to such terms and conditions as may be prescribed. In case the Central Government does not grant, within the said period of ninety days, a certificate or give prior permission, it shall communicate the reasons therefor to the applicant and that a person shall not be eligible for grant of certificate or giving prior permission, if his certificate has been suspended and such suspension of certificate continues on the date of making application.

Sub-section (4) of Section 12 provides following conditions for granting certificate of registration :—

- (a) the person making an application for registration or grant of prior permission under sub-section (1),—
  - (i) is not fictitious or benami;
  - (ii) has not been prosecuted or convicted for indulging in activities aimed at conversion through inducement or force, either directly or indirectly, from one religious faith to another;
  - (iii) has not been prosecuted or convicted for creating communal tension or disharmony in any specified district or any other part of the country;
  - (iv) has not been found guilty or diversion or mis-utilisation of its funds;

- (v) is not engaged or likely to engage in propagation of sedition or advocate violent methods to achieve its ends;
  - (vi) is not likely to use the foreign contribution for personal gains or divert it for undesirable purposes;
  - (vii) has not contravened any of the provisions of this Act;
  - (viii) has not been prohibited from accepting foreign contribution;
- (b) the person making an application for registration under sub-section (1) has undertaken reasonable activity in its chosen field for the benefit of the society for which the foreign contribution is proposed to be utilised;
- (c) the person making an application for giving prior permission under sub-section (1) has prepared a reasonable project for the benefit of the society for which the foreign contribution is proposed to be utilised;
- (d) in case the person being an individual, such individual has neither been convicted under any law for the time being in force nor any prosecution for any offence pending against him;
- (e) in case the person being other than an individual, any of its directors or office bearers has neither been convicted under any law for the time being in force nor any prosecution for any offence is pending against him;
- (f) the acceptance of foreign contribution by the person referred to in sub- section (1) is not likely to affect prejudicially—
- (i) the sovereignty and integrity of India; or
  - (ii) the security, strategic, scientific or economic interest of the State; or
  - (iii) the public interest; or
  - (iv) freedom or fairness of election to any Legislature; or
  - (v) friendly relation with any foreign State; or
  - (vi) harmony between religious, racial, social, linguistic, regional groups, castes or communities;
- (g) the acceptance of foreign contribution referred to in sub-section (1),—
- (i) shall not lead to incitement of an offence;
  - (ii) shall not endanger the life or physical safety of any person.

Where the Central Government refuses the grant of certificate or does not give prior permission, it shall record in its order the reasons therefor and furnish a copy thereof to the applicant. The Central Government may not communicate the reasons for refusal for grant of certificate or for not giving prior permission to the applicant under this section in cases where there is no obligation to give any information or documents or records or papers under the Right to Information Act, 2005.



*It may be noted that the certificate granted shall be valid for a period of five years and the prior permission shall be valid for the specific purpose or specific amount of foreign contribution proposed to be received, as the case may be.*

### Suspension of certificate

Section 13 (1) provides that where the Central Government, for reasons to be recorded in writing, is satisfied that pending consideration of the question of cancelling the certificate on any of the grounds mentioned in sub-section (1) of section 14, it is necessary so to do, it may, by order in writing, suspend the certificate for such period not exceeding one hundred and eighty days as may be specified in the order.

Further every person whose certificate has been suspended shall not receive any foreign contribution during the period of suspension of certificate. However, the Central Government, on an application made by such person, if it considers appropriate, allow receipt of any foreign contribution by such person on such terms and conditions as it may specify.

Every person whose certificate has been suspended shall utilise, in the prescribed manner, the foreign contribution in his custody with the prior approval of the Central Government.

### Cancellation of certificate

Section 14 empowers the Central Government to cancel the certificate. Accordingly, the Central Government may, if it is satisfied after making such inquiry as it may deem fit, by an order, cancel the certificate if —

- (a) the holder of the certificate has made a statement in, or in relation to, the application for the grant of registration or renewal thereof, which is incorrect or false; or
- (b) the holder of the certificate has violated any of the terms and conditions of the certificate or renewal thereof; or
- (c) in the opinion of the Central Government, it is necessary in the public interest to cancel the certificate; or
- (d) the holder of certificate has violated any of the provisions of this Act or rules or order made thereunder; or
- (e) if the holder of the certificate has not been engaged in any reasonable activity in its chosen field for the benefit of the society for two consecutive years or has become defunct.

Before passing an order of cancellation of certificate, the person concerned would be given a reasonable opportunity of being heard. Any person, whose certificate has been cancelled, shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate.

### Management of foreign contribution of person whose certificate has been cancelled

Section 15 provides that the foreign contribution and assets created out of the foreign contribution in the custody of every person whose certificate has been cancelled under section 14 shall vest in such authority as may be prescribed.

The authority may, if it considers necessary and in public interest, manage the activities of the person referred to in that sub-section for such period and in such manner, as the Central Government may direct. Such authority may utilise the foreign contribution or dispose of the assets created out of it in case adequate funds are not available for running such activity. The authority shall return the foreign contribution and the assets vested upon it to the person, if such person is subsequently registered under this Act.

### Renewal of certificate

*Every person who has been granted a certificate under section 12 shall have such certificate renewed within six months before the expiry of the period of the certificate [Section 16].*

### **Application for Renewal**

The application for renewal of the certificate shall be made to the Central Government in such form and manner and accompanied by such fee as may be prescribed. The Central Government shall renew the certificate, ordinarily within ninety days from the date of receipt of application for renewal of certificate subject to such terms and conditions as it may deem fit and grant a certificate of renewal for a period of five years. In case the Central Government does not renew the certificate within the said period of ninety days, it shall communicate the reasons therefor to the applicant. The Central Government may refuse to renew the certificate in case where a person has violated any of the provisions of this Act or rules made thereunder.

### **ACCOUNTS, INTIMATION, AUDIT AND DISPOSAL OF ASSETS**

#### ***Foreign contribution through scheduled bank***

Section 17 provides that every person who has been granted a certificate or given prior permission shall receive foreign contribution in a single account only through such one of the branches of a bank as he may specify in his application for grant of certificate.

However, such person may open one or more accounts in one or more banks for utilising the foreign contribution received by him. Further no funds other than foreign contribution shall be received or deposited in such account or accounts.

Every bank or authorised person in foreign exchange shall report to such authority as may be specified amount of foreign remittance; the source and manner in which the foreign remittance was received; and other particulars, in such form and manner as may be prescribed.

#### ***Intimation***

Section 18 requires every person who has been granted a certificate or given prior approval to provide within such time and in such manner as may be prescribed, an intimation to the Central Government, and such other authority as may be specified by the Central Government, as to the amount of each foreign contribution received by it, the source from which and the manner in which such foreign contribution was received, and the purposes for which, and the manner in which such foreign contribution was utilised by him.

Every person receiving foreign contribution is required to submit a copy of a statement indicating therein the particulars of foreign contribution received duly certified by officer of the bank or authorised person in foreign exchange and furnish the same to the Central Government along with the intimation.

#### ***Maintenance of accounts***

Section 19 requires every person who has been granted a certificate or given prior approval to maintain, in such form and manner as may be prescribed, an account of any foreign contribution received by him; and a record as to the manner in which such contribution has been utilised by him.

#### ***Order for Audit of accounts***

Section 20 provides that where any person who has been granted a certificate or given prior permission, fails to furnish any intimation within the time specified therefor or the intimation so furnished is not in accordance with law or if, after inspection of such intimation, the Central Government has any reasonable cause to believe that any provision of Act has been, or is being, contravened, the Central Government may, by general or special order, authorise such gazetted officer, holding a Group A post under the Central Government or any other officer or authority or organisation, as it may think fit, to audit any books of account

kept or maintained by such person and thereupon every such officer shall have the right to enter in or upon any premises at any reasonable hour, before sunset and after sunrise, for the purpose of auditing the said books of account and any information obtained from such audit shall be kept confidential and shall not be disclosed except for the purposes of the Act.

#### ***Intimation by candidate for election***

Section 21 requires every candidate for election, who had received any foreign contribution, at any time within one hundred and eighty days immediately preceding the date on which he is duly nominated as such candidate, shall give, within such time and in such manner as may be prescribed, an intimation to the Central Government or prescribed authority or both as to the amount of foreign contribution received by him, the source from which, and the manner in which, such foreign contribution was received and the purposes for which and the manner in which such foreign contribution was utilised by him.

#### ***Disposal of assets created out of foreign contribution***

Section 22 provides that where any person who was permitted to accept foreign contribution under this Act, ceases to exist or has become defunct, all the assets of such person shall be disposed of in accordance with the provisions contained in any law for the time being in force under which the person was registered or incorporated. In the absence of any such law, the Central Government may, having regard to the nature of assets created out of foreign contribution received under this Act, by notification, specify that all such assets shall be disposed off by such authority, as it may specify, in such manner and procedure as may be prescribed.

#### **INSPECTION, SEARCH AND SEIZURE**

Section 23 provides that if the Central Government has, for any reason, to be recorded in writing, any ground to suspect that any provision of this Act has been or is being, contravened by any political party; or any person; or any organisation; or any association, it may, by general or special order, authorise such gazetted officer, holding a Group A post under the Central Government or such other officer or authority or organisation, as it may think fit, to inspect any account or record maintained by such political party, person, organisation or association, as the case may be, and thereupon every such inspecting officer shall have the right to enter in or upon any premises at any reasonable hour, before sunset and after sunrise, for the purpose of inspecting the said account or record.

#### **Seizure of accounts or records**

Section 24 provides that if, after inspection of an account or record, the inspecting officer has any reasonable cause to believe that any provision of the Act or of any other law relating to foreign exchange has been, or is being, contravened, he may seize such account or record and produce the same before the court, authority or tribunal in which any proceeding is brought for such contravention. Further, the authorised officer shall return such account or record to the person from whom it was seized if no proceeding is brought within six months from the date of such seizure for the contravention disclosed by such account or record.

#### **Adjudication of confiscation**

Section 29 dealing with adjudication of confiscation, provides that any confiscation article or currency or security which is seized may be adjudged without limit, by the Court of Session within the local limits of whose jurisdiction the seizure was made; and subject to such limits as may be prescribed, by such officer, not below the rank of an Assistant Sessions Judge, as the Central Government may, by notification in the Official Gazette.

Section 30 provides that no order of adjudication of confiscation shall be made unless a reasonable opportunity of making a representation against such confiscation has been given to the person from whom any article or currency or security has been seized.

### **Appeal**

Section 31 deals with appeals and provides that any person aggrieved by any order made under section 29 may prefer an appeal, where the order has been made by the Court of Session, to the High Court to which such Court is subordinate; or where the order has been made by any officer specified, to the Court of Session within the local limits of whose jurisdiction such order of adjudication of confiscation was made, within one month from the date of communication to such person of the order.

Further the appellate court may, if it is satisfied that the appellant was prevented by sufficient cause from preferring the appeal within the said period of one month, allow such appeal to be preferred within a further period of one month, but not thereafter.

Every appeal preferred under this section shall be deemed to be an appeal from an original decree and the provisions of Order XLI of the First Schedule to the Code of Civil Procedure, 1908, shall, as far as may be, apply thereto as they apply to an appeal from an original decree.

### **Penalty and Punishment**

Section 34 prescribes for penalty on any person, on whom any prohibitory order has been served under section 10, pays, delivers, transfers or otherwise deals with, in any manner whatsoever, any article or currency or security, whether Indian or foreign, in contravention of such prohibitory order, he shall be punished with imprisonment for a term which may extend to three years, or with fine, or with both.

The court trying such contravention may also impose on the person convicted an additional fine equivalent to the market value of the article or the amount of the currency or security in respect of which the prohibitory order has been contravened by him or such part thereof as the court may deem fit.

Section 35 provides for punishment with imprisonment for a term which may extend to five years, or with fine, or with both for accepting, or assisting any person, political party or organisation in accepting, any foreign contribution or any currency or security from a foreign source, in contravention of any provision of this Act or any rule or order made thereunder.

### **Offences by companies**

Section 39 deals with offences by companies and provides that where an offence has been committed by a company, every person who, at the time the offence was committed, was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. However, such person shall not liable to any punishment if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence.

Further in the case an offence has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

### **Composition of certain offences**

Section 41 (1) provides that any offence punishable under this Act (whether committed by an individual or association or any officer or employee thereof), not being an offence punishable with imprisonment only, may, before the institution of any prosecution, be compounded by such officers or authorities and for such sums as the Central Government may, by notification in the Official Gazette, specify in this behalf.

Section 41(2) provides that any second or subsequent offence committed after the expiry of a period of three years from the date on which the offence was previously compounded, shall be deemed to be a first offence.

Every officer or authority shall exercise the powers to compound an offence, subject to the direction, control and supervision of the Central Government. Every application for the compounding of an offence shall be made to the officer or authority referred to in sub-section (1) in such form and manner alongwith such fee as may be prescribed. Where any offence is compounded before the institution of any prosecution, no prosecution shall be instituted in relation to such offence, against the offender in relation to whom the offence is so compounded.

Every officer or authority while dealing with an application for the compounding of an offence for a default in compliance with any provision of this Act which requires by an individual or association or its officer or other employee to obtain permission or file or register with, or deliver or send to, the Central Government or any prescribed authority any return, account or other document, may, direct, by order, if he or it thinks fit to do so, any individual or association or its officer or other employee to file or register with, such return, account or other document within such time as may be specified in the order.

### **LESSON ROUND UP**

- FCRA, 2010 regulate the acceptance and utilisation of foreign contribution or foreign hospitality by certain individuals or associations or companies and to prohibit acceptance and utilisation of foreign contribution or foreign hospitality for any activities detrimental to the national interest and for matters connected therewith or incidental thereto.
- The Act provides that persons having definite cultural, economic, educational, religious and social programmes should get themselves registered with the Government of India before accepting any 'foreign contribution'. In case a person falling in the above category is not registered with the Central Government, it can accept foreign contribution only after obtaining prior permission of the Central Government.
- Central Government is empowered to prohibit any person or organisation not specified in the Act from accepting any foreign contribution and to require any person or class of persons, not specified in it to obtain prior permission of the Central Government before accepting any foreign hospitality.
- Associations which were granted certificates of registration , such registration shall be valid for a period of five years.
- Any offence punishable under this act (whether committed by an individual or association or any officer or employee thereof), not being an offence punishable with imprisonment only, may, before the institution of any prosecution, be compounded by such officers or authorities and for such sums as the central government may, by notification in the official gazette, specify in this behalf.

### **SELF TEST QUESTIONS**

1. How does the FCRA, 2010 seeks to regulate the receipt of foreign contribution and foreign hospitality?
2. Define 'foreign contribution" and 'foreign source'.
3. Discuss the provisions of FCRA relevant to exemptions from acceptance of foreign contribution.
4. Explain the concept of 'organisation of a political nature' under the Foreign Contribution (Regulation) Act, 2010.
5. Discuss the powers of Central Government under FCRA to prohibit receipt of foreign contribution.



# Lesson 2

## FOREIGN TRADE POLICY AND PROCEDURE

### Section I

#### LESSON OUTLINE

- Broad Framework of Foreign Trade Policy
- General Provisions regarding exports and imports
- Duration and Applicability of FTP
- Transitional Arrangements
- Market Diversification
- Technological Upgradation
- IEC Number
- Promotional Measures
- Special Focus Initiative
- Board of Trade
- Market Access Initiative (MAI)
- Market Development Assistance (MDA)
- Export and Trading Houses
- Focus Product Scheme
- Focus Market Scheme
- Duty exemption schemes
- Export Oriented Undertaking
- Software Technology Park
- Bio-Technology Park

#### LEARNING OBJECTIVES

With a view to make India a major player in world trade, the Government has taken an all encompassing, comprehensive view for the overall development of the country's foreign trade. Economic reforms and globalisation of the Indian economy has been the guiding factor in formulating the trade policies. In India, the main legislation concerning foreign trade is the Foreign Trade (Development and Regulation) Act, 1992. The Act provides for the development and regulation of foreign trade by facilitating imports into, and augmenting exports from, India and for matters connected therewith or incidental thereto.

In exercise of the powers conferred by the Foreign Trade (Development and Regulation) Act, 1992, Central Government notifies trade policy on a regular basis with certain underlined objectives. The trade policies were based on the objectives of self-reliance and self-sufficiency and driven by factors like export led growth, improving efficiency and competitiveness of the Indian industries, etc. In the overall context of development perspective, the Government has adopted Foreign Trade Policy as an integrated approach to the developmental requirements of India's foreign trade.

This section deals with Foreign Trade Policy 2009-2014 incorporating provisions relating to export and import of goods and services.

In exercise of powers conferred by Section 5 of the Foreign Trade (Development & Regulation) Act, 1992 the Central Government notified the Foreign Trade Policy, 2009-2014. The Foreign Trade Policy 2009-2014 (FTP), incorporating provisions relating to export and import of goods and services, came into force with effect from 27th August, 2009 and shall remain in force upto 31st March, 2014 unless otherwise specified.

## INTRODUCTION

The short term objective of Foreign Trade policy is to arrest and reverse the declining trend of exports and to provide additional support especially to those sectors which have been hit badly by recession in the developed world. By 2014, it expects to double India's exports of goods and services. The long term policy objective for the Government is to double India's share in global trade by 2020.

In order to meet these objectives, the Government would follow a mix of policy measures including fiscal incentives, institutional changes, procedural rationalization, enhanced market access across the world and diversification of export markets. Improvement in infrastructure related to exports; bringing down transaction costs, and providing full refund of all indirect taxes and levies, would be the three pillars, which will support to achieve the target.

To provide adequate confidence to exporters to maintain their market presence even in a period of stress, a special thrust would be provided to employment intensive sectors, especially in the fields of textile, leather, handicrafts, etc.

In the era of global competitiveness, there is an imperative need for Indian exporters to upgrade their technology and reduce their costs. Accordingly, an important element of the Foreign Trade Policy is to help exporters for technological upgradation, which is sought to be achieved by promoting imports of capital goods for certain sectors under EPCG at zero percent duty.

The Government recognizes exporters based on their export performance and they are called 'status holders'. For technological upgradation of the export sector, these status holders will be permitted to import capital goods duty free (through Duty Credit Scrips), of specified product groups. This will help them to upgrade their technology and reduce cost of production.

For upgradation of export sector infrastructure, 'Towns of Export Excellence' and units located therein would be granted additional focused support and incentives.

## Duration and Applicability of Foreign Trade Policy

In exercise of powers conferred by Section 5 of the Foreign Trade (Development & Regulation) Act, 1992 (No.22 of 1992) the Central Government notified the Foreign Trade Policy, 2009-2014. The Foreign Trade Policy 2009-2014 (FTP), incorporating provisions relating to export and import of goods and services, came into force with effect from 27th August, 2009 and shall remain in force upto 31st March, 2014 unless otherwise specified. All exports and imports upto 26th August 2009 would however be governed by the Foreign Trade Policy 2004-2009.

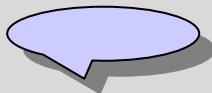
## Transitional Arrangements

Authorisation issued before commencement of Foreign Trade Policy shall continue to be valid for the purpose and duration for which such Authorisation was issued, unless otherwise stipulated.

In case an export or import that is permitted freely under erstwhile Foreign Trade Policy is subsequently subjected to any restriction or regulation, such export or import will ordinarily be permitted notwithstanding such restriction or regulation, unless otherwise stipulated, provided that shipment of export or import is made within original validity with respect to available balance and time period of an irrevocable commercial letter of credit, established before date of imposition of such restriction. However for operationalizing such irrevocable commercial letter of credit the applicant shall have to register the Letter of Credit and contract with the concerned Regional Authority within 15 days of the issue of any such restriction or regulation.

## SPECIAL FOCUS INITIATIVES

*With a view to continuously increasing India's percentage share of global trade and expanding employment opportunities, certain special focus initiatives have been identified/continued for:*



- *Market Diversification*
- *Technological Upgradation*
- *Support to status holders*
- *Agriculture, Handlooms*
- *Handicraft*
- *Gems & Jewellery*
- *Leather*
- *Marine*
- *Electronics and IT Hardware manufacturing Industries*
- *Green products*
- *Exports of products from North-East*
- *Sports Goods and Toys sectors.*

The Government shall make concerted efforts to promote exports in these sectors by specific sectoral strategies to be notified from time to time.

### Market Diversification

To insulate Indian exports from the decline in demand from developed countries, the Policy focuses on diversification of Indian exports to other markets, specially those located in Latin America, Africa, parts of Asia and Oceania. To achieve diversification of Indian exports, following initiatives have been taken under this Policy.

- (a) 29 new countries have been included within the ambit of Focus Market Scheme.
- (b) The incentives provided under Focus Market Scheme have been increased from 2.5% to 3%.
- (c) There has been a significant increase in the outlay under 'Market Linked Focus Product Scheme' by inclusion of more markets and products. This ensures support for exports to all countries in Africa and Latin America, and Major Asian Market like China and Japan.

### Technological Upgradation

To usher in the next phase of export growth, India needs to move up in the value chain of export goods. This objective is sought to be achieved by encouraging technological upgradation of India's export sector. A number of initiatives have been taken to focus on technological upgradation; such initiatives include:

- (a) Export Promotion Capital Goods Scheme at zero duty has been introduced for certain engineering products, electronic products, basic chemicals and pharmaceuticals, apparel and textiles, plastics, handicrafts, chemicals and allied products and leather and leather products.
- (b) The existing 3% EPCG Scheme has been considerably simplified, to ease its usage by the exporters.

- (c) To encourage value added manufacture export, a minimum 15% value addition on imported inputs under Advance Authorisation Scheme has been stipulated.
- (d) A number of products including automobiles and other engineering products have been included for incentives under Focus Product, and Market Linked Focus Product Schemes.
- (e) Steps to encourage Project Exports shall be taken.

### **Support to status holders**

Status Holders contribute approx. 60% of India's goods exports. To incentivise and encourage the status holders, as well as to encourage Technological upgradation of export production, additional duty credit scrip @ 1% of the FOB of past export has been granted for specified product groups including leather, specific sub sectors in engineering, textiles, plastics, handicrafts and jute. This duty credit scrip can be used for import of capital goods by these status holders. The imported capital goods shall be subject to actual user condition.

### **Agriculture and Village Industry**

- (a) Vishesh Krishi and Gram Udyog Yojana
- (b) Capital goods imported under Export Promotion Capital Goods have been permitted to be installed anywhere in Agri Export Zone.
- (c) Import of restricted items, such as panels, have been allowed under various export promotion schemes.
- (d) Import of inputs such as pesticides have been permitted under Advance Authorisation for agro exports.
- (e) New towns of export excellence with a threshold limit of Rs 150 crore have been notified.
- (f) Certain specified flowers, fruits and vegetables are entitled to special duty credit scrip, in addition to the normal benefit under VKGUY.

### **Handlooms**

- (a) Specific funds have been earmarked under Market Access Initiative (MAI) / Market Development Assistance (MDA) Scheme for promoting handloom exports.
- (b) Duty free import entitlement of specified trimmings and embellishments has been fixed as 5% of FOB value of exports during previous financial year.
- (c) Duty free import entitlement of hand knotted carpet samples has been fixed as 1% of FOB value of exports during previous financial year.
- (d) Duty free import of old pieces of hand knotted carpets on consignment basis for re-export after repair has been permitted.
- (e) New towns of export excellence with a threshold limit of Rs. 150 crore have been notified.
- (f) Machinery and equipment for effluent treatment plants has been exempt from customs duty.

### **Handicrafts**

- (a) Duty free import entitlement of tools, trimmings and embellishments has been fixed as 5% of FOB value of exports during previous financial year. Entitlement is broad banded, and shall extend also to merchant exporters tied up with supporting manufacturers.

- (b) Handicraft Export Promotion Council has been authorized to import trimmings, embellishments and consumables on behalf of those exporters for whom directly importing may not be viable.
- (c) Specific funds have been earmarked under MAI & MDA Schemes for promoting Handicraft exports.
- (d) Countervailing Duty has been exempted on duty free import of trimmings, embellishments and consumables.
- (e) New towns of export excellence with a reduced threshold limit of Rs 150 crore have been notified.
- (f) Machinery and equipment for effluent treatment plants are exempt from customs duty.
- (g) All handicraft exports would be treated as special Focus products and entitled to higher incentives.

### Gems & Jewellery

- (a) Import of gold of 8 carets and above has been allowed under replenishment scheme subject to import being accompanied by an Assay Certificate specifying purity, weight and alloy content.
- (b) Duty Free Import Entitlement (based on FOB value of exports during previous financial year) of Consumables and Tools, for:
  - 1. Jewellery made out of:
    - (a) Precious metals (other than Gold & Platinum)
    - (b) Gold and Platinum
    - (c) Rhodium finished Silver
  - 2. Cut and Polished Diamonds
- (c) Duty free import entitlement of commercial samples has been fixed as Rs. 300,000.
- (d) Duty free re-import entitlement for rejected jewellery has been fixed as 2% of FOB value of exports.
- (e) Import of Diamonds on consignment basis for Certification/ Grading & re-export by the authorized offices/agencies of Gemological Institute of America (GIA) in India or other approved agencies will be permitted.
- (f) Personal carriage of Gems & Jewellery products in case of holding/ participating in overseas exhibitions increased to US\$ 5 million and to US\$ 1 million in case of export promotion tours.
- (g) Extension in number of days for re-import of unsold items in case of participation in an exhibition in USA increased to 90 days.
- (h) In an endeavour to make India a diamond international trading hub, the Government proposes to establish "Diamond Bourse (s)".

### Leather and Footwear

- (a) Duty free import entitlement of specified items has been fixed as 3% of FOB value of exports of leather garments during preceding financial year.
- (b) Duty free entitlement for import of trimmings, embellishments and footwear components for footwear (leather as well as synthetic), gloves, travel bags and handbags has been fixed as 3% of FOB value of exports of previous financial year. Such entitlement also cover packing material, such as printed and non printed shoeboxes, small cartons made of wood, tin or plastic materials for packing footwear.

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- (c) Machinery and equipment for Effluent Treatment Plants have been exempt from basic customs duty.
- (d) Re-export of unsuitable imported materials such as raw hides & skins and wet blue leathers is permitted.
- (e) Countervailing Duty is exempted on lining and interlining material.
- (f) Countervailing Duty is exempted on raw, tanned and dressed fur skins falling under Chapter 43 of ITC (HS).
- (g) Re-export of unsold hides, skins and semi finished leather have been allowed from Public Bonded warehouse without payment of export duty.

### Marine Sector

- (a) Imports for technological upgradation under EPCG in fisheries sector (except fishing trawlers, ships, boats and other similar items) exempted from maintaining average export obligation.
- (b) Duty free import of specified specialised inputs / chemicals and flavouring oils has been allowed to the extent of 1% of FOB value of preceding financial year's export.
- (c) To allow import of monofilament longline system for tuna fishing at a concessional rate of duty and Bait Fish for tuna fishing at Nil duty.
- (d) A self removal procedure for clearance of seafood waste is applicable subject to prescribed wastage norms.
- (e) Marine sector included for benefits under zero duty and EPCG Scheme.

### Electronics and IT Hardware Manufacturing Industries

- (a) Expedited clearance of approvals required from Director General Foreign Trade shall be ensured.
- (b) Exporters/Associations would be entitled to utilize Market Access Initiative (MAI) & Market Development Assistance (MDA) Schemes for promoting Electronics and IT Hardware Manufacturing industry exports.

### Sports Goods and Toys

- (a) Duty free import of specified specialised inputs allowed to the extent of 3 % of FOB value of preceding financial year's export.
- (b) Sports goods and toys shall be treated as a Priority sector under Market Access Initiative (MAI) & Market Development Assistance (MDA) Scheme. Specific funds would be earmarked under MAI/ MDA Scheme for promoting exports from this sector.
- (c) Applications relating to Sports Goods and Toys have been considered for fast track clearance by DGFT.
- (d) Sports Goods and Toys are treated as special focus products and entitled to higher incentives.

### Green products and technologies

India aims to become a hub for production and export of green products and technologies. To achieve this objective, special initiative will be taken to promote development and manufacture of such products and technologies for exports. To begin with, focus would be on items relating to transportation, solar and wind power generation and other products as may be notified which will be incentivized under Reward Schemes of Foreign Trade Policy.

## **Incentives for Exports from the North Eastern Region**

In order to give a fillip to exports of products from the north-eastern States, notified products of this region would be incentivized under Reward Schemes of Foreign Trade Policy.

## **BOARD OF TRADE**

Board of Trade has a clear and dynamic role in advising government on relevant issues connected with Foreign Trade. Board of Trade has following terms of reference:

- (i) Advising Government on Policy measures for preparation and implementation of both short and long term plans for increasing exports in the light of emerging national and international economic scenarios;
- (ii) Reviewing export performance of various sectors, identify constraints and suggest industry specific measures to optimize export earnings;
- (iii) Examining existing institutional framework for imports and exports and suggest practical measures for further streamlining to achieve desired objectives;
- (iv) Reviewing policy instruments and procedures for imports and exports and suggest steps to rationalize and channelize such schemes for optimum use;
- (v) Examining issues which are considered relevant for promotion of India's foreign trade, and to strengthen international competitiveness of Indian goods and services; and
- (vi) Commissioning studies for furtherance of above objectives.

## **Board of Trade - Composition and Meeting**

Commerce & Industry Minister to be the Chairman of the Board of Trade (BOT). Government shall also nominate upto 25 persons, of whom at least 10 to be experts in trade policy. In addition, Chairmen of recognized Export Promotion Councils and President or Secretary-Generals of National Chambers of Commerce to be ex-officio members. BOT is required to meet at least once every quarter.

## **GENERAL PROVISIONS REGARDING IMPORTS AND EXPORTS**

Exports and Imports have been made free, except where regulated by Foreign Trade Policy or any other law for the time being in force. The item wise export and import policy would however be, as specified in ITC (HS) notified by Director General of Foreign Trade, as amended from time to time. Every exporter or importer is required to comply with the provisions of Foreign Trade (Development & Regulation) Act, the Rules and Orders made there-under, Foreign Trade Policy and terms and conditions of any Authorisation granted to him. All imported goods have also been made subject to domestic Laws, Rules, Orders, Regulations, technical specifications, environmental and safety norms as applicable to domestically produced goods. The import or export of rough diamonds is not permitted unless accompanied by Kimberley Process (KP) Certificate as specified by Gem & Jewellery Export Promotion Council (GJEPC).

## **Interpretation of Policy**

The Director General of Foreign Trade has been empowered to decide on any question or doubt arises in respect of interpretation of any provision contained in Foreign Trade Policy, or classification of any item in ITC (HS) or procedures, or Schedule of Duty Entitlement Passbook Rates. The FTP further stipulate that any question or doubt touching upon the content, scope or issue of an authorization there under should be referred to Director General of Foreign Trade whose decision thereon shall be final and binding.

***Who is empowered to decide questions arising in respect of interpretation of FTP?***

DGFT, The Foreign Trade Policy 2009-14 empowers the Director General of Foreign Trade to decide on any question or doubt arising in respect of the interpretation of any provision contained in the Policy, or regarding the classification of any item in the ITC(HS) or procedures, any scheme, or Schedule of DEPB Rate.



**Procedure**

The Director General of Foreign Trade may, specify procedure to be followed for an exporter or importer or by any licensing or any other competent authority for purpose of implementing provisions of Foreign Trade (Development & Regulation ) Act, the Rules and the Orders made there under and Foreign Trade Policy. Such procedures shall be published by means of a Public Notice, and may, in like manner, be amended from time to time.

**Exemption from Policy/Procedure**

The Director General of Foreign Trade has been empowered to pass such orders or grant such relaxation or relief, as he may deem fit and proper, on grounds of genuine hardship and adverse impact on trade. DGFT may also , in public interest, exempt any person or class or category of persons from any provision of Foreign Trade Policy or any procedure and may, while granting such exemption, impose such conditions as he may deem fit.

**Principles of Restriction**

DGFT has been empowered to adopt and enforce, through a notification, any measure necessary for:

- (i) Protection of public morals.
- (ii) Protection of human, animal or plant life or health.
- (iii) Protection of patents, trademarks and copyrights and the prevention of deceptive practices.
- (iv) Prevention of use of prison labour.
- (v) Protection of national treasures of artistic, historic or archaeological value.
- (vi) Conservation of exhaustible natural resources.
- (vii) Protection of trade of fissionable material or material from which they are derived; and
- (viii) Prevention of traffic in arms, ammunition and implements of war.

**Export and Import of Restricted Goods/Services**

The Foreign Trade Policy allows the export or import of any goods/services, which is restricted only in accordance with an Authorisation or in terms of a public notice issued in this behalf.

**Terms and Conditions of a licence/Certificate/Permission/ Authorisation**

Every Authorisation shall be valid for prescribed period of validity and shall contain such terms and conditions as may be specified by Regional Authority which may include:

- (a) Quantity, description and value of goods;
- (b) Actual User condition;

- (c) Export obligation;
- (d) Value addition to be achieved; and
- (e) Minimum export / import price.

### Authorisation/Licence/Certificate/Permission not a Right

No person may claim an Authorisation as a right and Director General of Foreign Trade or Regional Authority have been empowered to refuse to grant or renew the same in accordance with provisions of Foreign Trade (Development & Regulation) Act, Rules made there under and Foreign Trade Policy.

#### **Whether every licence valid for a specified period under FTP?**

Yes, Foreign Trade Policy 2009-14 provides that every licence/certificate/permission/ authorisation shall be valid for the period of validity specified in the licence/certificate/ permission/authorisation shall contain such terms and conditions as may be specified by the licensing authority.



### Penalty

If an Authorisation holder violates any condition of such Authorisation or fails to fulfill export obligation, he shall be liable for action in accordance with Foreign Trade (Development & Regulation) Act, the Rules and Orders made there under, Foreign Trade Policy and any other law for time being in force.

### State Trading

Any goods, import or export of which is governed through exclusive or special privileges granted to State Trading Enterprise(s), may be imported or exported by STE(s) as per conditions specified in ITC (HS). DGFT may, however, grant an Authorisation to any other person to import or export any of these goods. Such STE(s) shall make any such purchases or sales involving imports or exports solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale in a non discriminatory manner and shall afford enterprises of other countries adequate opportunity, in accordance with customary business practices, to compete for participation in such purchases or sales.

### Importer-Exporter Code (IEC) Number

The Foreign Trade Policy prohibits export or import by any person without an IEC number unless specifically exempted. An IEC number is granted on application by competent authority in accordance with specified procedure.

### IEC No: Exempted Categories

The following categories of importers or exporters have been exempted from obtaining IEC number:

- (i) Importers covered by clause 3(1) [except sub-clauses (e) and (l)] and exporters covered by clause 3(2) [except sub-clauses (i) and (k)] of the Foreign Trade (Exemption from application of Rules in certain cases) Order, 1993.
- (ii) Ministries/Departments of the Central or State Government.

- (iii) Persons importing or exporting goods for personal use not connected with trade or manufacture or agriculture.
- (iv) Persons importing/exporting goods from/to Nepal/Myanmar through Indo-Myanmar border areas provided the CIF value of a single consignment does not exceed Indian ₹ 25,000.

However, the exemption from obtaining Importer-Exporter Code (IEC) is not applicable for the export of Special Chemicals, Organisms, Materials, Equipments and Technologies (SCOMET) except in the case of exports by Ministeries/Departments of the Central/State Government.

- (vi) The FTP allows the following permanent IEC numbers to be used by the categories of importers/exporters mentioned against them for import/ export purposes.

<i>S.No.</i>	<i>Code Number</i>	<i>Categories of Importers/Exporters</i>
<i>1</i>	<i>2</i>	<i>3</i>
1.	0100000011	All Ministries/Departments of the Central Government and agencies wholly or partially owned by them.
2.	0100000029	All Ministries/Departments of the State Government and agencies wholly or partially owned by them.
3.	0100000037	Diplomatic personnel, Counselor officers in India and the officials of the UNO and its specialised agencies.
4.	0100000045	Indians returning from/going abroad and claiming benefit under the Baggage Rules.
5.	0100000053	Persons/Institutions/Hospitals importing or exporting goods for personnel use, not connected with trade or manufacture or agriculture.
6.	0100000061	Persons importing/ exporting goods from/to Nepal provided the CIF value of a single consignment does not exceed Indian Rupees 25000/-.
7.	0100000070	Persons importing/ exporting goods from/to Myanmar through Indo-Myanmar border areas provided the CIF value of a single consignment does not exceed Indian Rupees 25000/-.
8.	0100000088	Ford Foundation
9.	0100000096	Importers importing goods for display or use in fairs/exhibitions or similar events under the provisions of ATA carnet.
10.	0100000100	Director, National Blood Group Reference Laboratory, Bombay or their authorized offices.
11.	0100000126	Individuals/Charitable Institutions/ Registered NGOs importing goods, which have been exempted from Customs duty under the Notification issued by Ministry of Finance for bonafide use by the victims affected by natural calamity.

#### **Application for Grant of IEC Number**

An application for grant of IEC number is required to be made in the prescribed form alongwith specified documents, by the Registered/Head Office of the applicant to the Regional authority under whose jurisdiction, the Registered office in case of company and Head office in case of others, falls. In case of STP/ EHTP/ BTP units, the Regional Offices of the DGFT having jurisdiction over the district in which the Registered/ Head Office of the STP unit is located has been empowered to issue or amend the IECs. An IEC

number allotted to an applicant remains valid for all its branches/divisions/ units/factories as indicated in the format of IEC.

### **Duplicate Copy of IEC No.**

In case the IEC Number is lost or misplaced, the issuing authority may consider requests for grant of a duplicate copy of IEC number, if accompanied by an affidavit.

### **Surrender of IEC No.**

If an IEC holder does not wish to operate the allotted IEC number, the same may be surrendered by informing the issuing authority. On receipt of such intimation, the issuing authority immediately cancel the same and electronically transmit it to DGFT for onward transmission to the Customs and Regional Authorities.

## **PROMOTIONAL MEASURES**

### *Assistance to States for Developing Export Infrastructure and Allied Activities (ASIDE)*

The Department of Commerce has administered the scheme called Assistance to States for Developing Export Infrastructure and Allied Activities (ASIDE). The objective of scheme is to establish a mechanism for involving the State Governments to participate in funding of infrastructure critical for growth of exports by providing export performance linked financial assistance to them. The activities aimed at development of infrastructure for exports can be funded from the scheme provided such activities have overwhelming export content and their linkage with exports is full established. The specific purposes for which funds allocated under the Scheme can be sanctioned and utilized are as follows:

- Creation of new Export Promotion Industrial Parks/Zones (SEZs/Agri Business Zones) and augmenting facilities in the existing ones.
- Setting up of electronics and other related infrastructure in export conclave.
- Equity participation in infrastructure projects including the setting up of SEZs.
- Meeting requirements of capital outlay of EPIPs/ EPZs/SEZs.
- Development of complementary infrastructure such as, roads connecting the production centres with the ports, setting up of Inland Container Depots and Container Freight Stations.
- Stabilizing power supply through additional transformers and islanding of export production centre etc.
- Development of minor ports and jetties to serve export purpose.
- Assistance for setting up Common Effluent Treatment facilities and
- Any other activity as may be notified by Department of Commerce.

### **Market Access Initiative (MAI)**

Under MAI scheme, financial assistance is provided for export promotion activities on focus country, focus product basis. Financial assistance is available for Export Promotion Councils (EPCs), Industry and Trade Associations (ITAs), Agencies of State Government, Indian Commercial Missions (ICMs) abroad and other national level institutions/eligible entities as may be notified.

A whole range of activities can be funded under MAI scheme. These include, amongst others,

- Market studies/surveys,

- Setting up of showroom / warehouse,
- Participation in international trade fairs,
- Displays in International departmental stores,
- Publicity campaigns,
- Brand promotion,
- Reimbursement of registration charges for pharmaceuticals and expenses for carrying out clinical trials etc., in fulfillment of statutory requirements in the buyer country,
- Testing charges for engineering products abroad,
- Assistance for contesting Anti Dumping litigations etc.

Each of these export promotion activities can receive financial assistance from Government ranging from 25% to 100% of total cost depending upon activity and implementing agency.

### **Market Development Assistance (MDA)**

Under MDA Scheme, financial assistance is provided for a range of export promotion activities implemented by Export Promotion Councils and Trade Promotion Organizations on the basis of approved annual action plans. The scheme is administered by Department of Commerce. Assistance includes, amongst others, participation in:

- Trade Fairs and Buyer Seller meets abroad or in India, and
- Export promotions seminars.
- Financial assistance with travel grant is available to exporters traveling to focus areas, viz., Latin America, Africa, CIS region, ASEAN countries, Australia and New Zealand. In other areas, financial assistance without travel grant is available.

MDA assistance is available for exports having an annual export turnover as prescribed in MDA guidelines.

### **Meeting expenses for statutory compliances in buyer country for Trade Related Matters**

Department Of Commerce provides for reimbursement of charges/expenses for fulfilling statutory requirements in the buyer country, including registration charges for product registration for pharmaceuticals, bio-technology and agro-chemicals products on recommendation of Export Promotion Councils. Financial assistance is also provided for contesting litigation(s) in the foreign country concerning restrictions/anti dumping duties etc. on particular product(s) of Indian origin, as provided under the Market Access Initiative (MAI) Scheme of Department of Commerce.

### **Towns of Export Excellence (TEE)**

A number of towns have emerged as dynamic industrial clusters contributing handsomely to India's exports. It is necessary to grant recognition to these industrial clusters with a view to maximizing their potential and enabling them to move higher in the value chain and tap new markets.

Selected towns producing goods of Rs. 750 Crore or more has been notified as TEE based on potential for growth in exports. However for TEE in Handloom, Handicraft, Agriculture and Fisheries sector, threshold limit would be Rs 150 Crores.

- (i) Recognized associations of units will be provided financial assistance under MAI scheme, on priority basis, for export promotion projects for marketing, capacity building and technological services.

- (ii) Common Service Providers in these areas shall be entitled for Export Promotion Capital Goods scheme.
- (iii) The projects received from TEEs shall be accorded priority by SLEPC for financial assistance under ASIDE.

### **Brand Promotion and Quality**

IBEF (originally called India Brand Equity Fund and later renamed as India Brand Equity Foundation) was set up by the Ministry of Commerce on 11 th July, 1996, with the primary objective to promote and create international awareness of the “Made in India” label in markets overseas. IBEF aims to promote India as a business opportunity by creating positive economic perceptions of India globally as well as effectively present the India business perspective and leverage business partnerships in a globalised market-place.

Department of Commerce provides funds for capacity building for up-gradation of quality to national level Institutions and Export Promotion Councils to organize training programmes for the skill improvement of the exporters for quality up-gradation, reduction in rejection, product improvement etc. as provided under the Market Access Initiative (MAI) Scheme of Department of Commerce.

### **Test Houses**

Central Government will assist in modernization and up gradation of test houses and laboratories to bring them at par with international standards.

### **Quality Complaints/Disputes**

Regional Sub-Committee on Quality Complaints (RSCQC) set up at Regional Offices of the Directorate shall investigate quality complaints received from foreign buyers.

### **Trade Disputes affecting Trade Relations**

If it comes to Director General of Foreign Trade's notice or he has reason to believe that an export or import has been made in a manner that

- (i) is gravely prejudicial to trade relations of India with any other country; and / or
- (ii) is gravely prejudicial to interest of other persons engaged in exports or imports; and/or
- (iii) has brought disrepute to the country;

DGFT may take action against such exporter or importer in accordance with Foreign Trade (Development & Regulation) Act, Rules and Orders made there-under and Foreign Trade Policy.

### **EXPORT AND TRADING HOUSES**

Merchant as well as Manufacturer Exporters, Service Providers, Export Oriented Units (EOUs) and Units located in Special Economic Zones (SEZs), Agri Export Zones (AEZs), Electronic Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio- Technology Parks (BTPs) shall be eligible for recognition as a status holder.

Applicant shall be categorized depending on his total FOB (FOR - for deemed exports) export performance during current plus previous three years (taken together) upon exceeding limit below. For Export House (EH)

## 80 EP-ECL

Status, export performance is necessary in at least two out of four years (i.e., current plus previous three years).

Status Category	Export Performance FOB / FOR Value (Rupees in Crores)
Export House (EH)	20
Star Export House (SEH)	100
Trading House (TH)	500
Star Trading House (STH)	2500
Premier Trading House (PTH)	7500

### Privileges of Export and Trading House Status Holders are as follows:

- (i) Authorization and Customs Clearances for both imports and exports on self-declaration basis;
- (ii) Fixation of Input-Output norms on priority within 60 days;
- (iii) Exemption from compulsory negotiation of documents through banks. Remittance/Receipts, however, would be received through banking channels;
- (iv) 100% retention of foreign exchange in EEFC account;
- (v) Exemption from furnishing of BG in Schemes under FTP;
- (vi) SEHs and above shall be permitted to establish Export Warehouses, as per DoR guidelines.
- (vii) For status holders, a decision on conferring of ACP Status shall be communicated by Customs within 30 days from receipt of application with Customs.
- (viii) As an option, for Premier Trading House (PTH), the average level of exports under EPCG Scheme shall be the arithmetic mean of export performance in last 5 years, instead of 3 years.
- (ix) Status Holders of specified sectors shall be eligible for Status Holder Incentive Scrip under FTP.
- (x) Status Holders of Agri. Sector (Chapter 1 to 24) shall be eligible for Agri. Infrastructure Incentive Scrip.

### FOCUS MARKET SCHEME (FMS)

Objective of focus market scheme is to offset high freight cost and other externalities to select international markets with a view to enhance India's export competitiveness in these countries. Exporters of all products to notified countries (as in shall be entitled for Duty Credit Scrip equivalent to 3 % of FOB value of exports (in free foreign exchange) for exports made from 27.8.2009 onwards.

### FOCUS PRODUCT SCHEME (FPS)

Objective of focus product scheme is to incentivise export of such products which have high export intensity / employment potential, so as to offset infrastructure inefficiencies and other associated costs involved in marketing of these products. Exports of notified products to all countries (including SEZ units) shall be entitled for Duty Credit scrip equivalent to 2 % of FOB value of exports (in free foreign exchange) for exports made from 27.8.2009 onwards.

## DUTY EXEMPTION & REMISSION SCHEMES

Duty exemption schemes enable duty free import of inputs required for export production. Duty Exemption Schemes consist of (a) Advance Authorisation scheme and (b) Duty Free Import Authorisation (DFIA) scheme. A Duty Remission Scheme enables post export replenishment / remission of duty on inputs used in export product. Duty Remission Schemes consist of Duty Drawback (DBK) Scheme. Goods exported under Advance Authorisation/DFIA/DEPB may be re-imported in same or substantially same form subject to DoR specified conditions.

### EXPORT ORIENTED UNITS (EOUs), ELECTRONICS HARDWARE TECHNOLOGY PARKS (EHTPs), SOFTWARE TECHNOLOGY PARKS (STPs) AND BIO-TECHNOLOGY PARKS (BTPs)

Units undertaking to export their entire production of goods and services (except permissible sales in DTA), may be set up under the Export Oriented Unit (EOU) Scheme, Electronics Hardware Technology Park (EHTP) Scheme, Software Technology Park (STP) Scheme or Bio-Technology Park (BTP) Scheme for manufacture of goods, including repair, re-making, reconditioning, reengineering and rendering of services. Trading units are not covered under these schemes.

#### ***Export and Import of Goods by EOUs, EHTPs, STPs and BTPs***

(a) An EOU/EHTP/STP/BTP unit may export all kinds of goods and services except items that are prohibited in ITC (HS). Export of Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET) shall be subject to fulfillment of the conditions indicated in ITC(HS). Procurement and supply of export promotion material like brochure/literature, pamphlets, hoardings, catalogues, posters etc. upto a maximum value limit of 1.5% of FOB value of previous years exports shall also be allowed.

(b) An EOU/EHTP/STP/BTP unit may import and/ or procure, from DTA or bonded warehouses in DTA/ international exhibition held in India, without payment of duty, all types of goods, including capital goods, required for its activities, provided they are not prohibited items of import in the ITC (HS). Any permission required for import under any other law shall be applicable. Units shall also be permitted to import goods including capital goods required for approved activity, free of cost or on loan/lease from clients. Import of capital goods will be on a self certification basis. Goods imported by a unit shall be with actual user condition and shall be utilized for export production.

(c) State Trading regime shall not apply to EOU manufacturing units. However, in respect of Chrome Ore / Chrome concentrate, State Trading Regime as stipulated in export policy of these items, will be applicable to EOUs.

(d) EOU/EHTP/STP/BTP units may import/procure from DTA, without payment of duty, certain specified goods for creating a central facility. Software EOU/DTA units may use such facility for export of software.

(e) An EOU engaged in agriculture, animal husbandry, aquaculture, floriculture, horticulture, pisciculture, viticulture, poultry or sericulture may be permitted to remove specified goods in connection with its activities for use outside bonded area.

(f) Gems and jewellery EOUs may source gold/silver/ platinum through nominated agencies on loan/outright purchase basis. Units obtaining gold/ silver/ platinum from nominated agencies, either on Loan basis or outright purchase basis shall export gold/ silver/platinum within 90 days from date of release.

(g) EOU/EHTP/STP/BTP units, other than service units, may export to Russian Federation in Indian Rupees against repayment of State Credit / Escrow Rupee Account of buyer subject to RBI clearance, if any.

(h) Procurement and export of spares/components, upto 5 % of FOB value of exports, may be allowed to same consignee/buyer of the export article, subject to the condition that it shall not count for NFE and direct tax benefits.

(i) BoA may allow, on a case to case basis, requests of EOU/EHTP/STP/BTP units in sectors other than Gems & Jewellery, for consolidation of goods related to manufactured articles and export thereof along with manufactured article. Such goods may be allowed to be imported/procured from DTA by EOU without payment of duty, to the extent of 5 % FOB value of such manufactured articles exported by the unit in preceding financial year. Details of procured/imported goods and articles manufactured by the EOU will be listed separately in the export documents. In such cases, value of procured/imported goods will not be taken into account for calculation of NFE, DTA sale entitlement & profits accruing out of such procured/imported goods will not be eligible for income tax benefits. Such procured/ imported goods shall not be allowed to be sold in DTA. BoA may also specify any other conditions.

### **LESSON ROUND UP**

- The short term objective of Foreign Trade policy is to arrest and reverse the declining trend of exports and to provide additional support especially to those sectors which have been hit badly by recession in the developed world. By 2014, it expects to double India's exports of goods and services. The long term policy objective for the Government is to double India's share in global trade by 2020.
- In exercise of powers conferred by Section 5 of the Foreign Trade (Development & Regulation) Act, 1992 (No.22 of 1992) the Central Government notified the Foreign Trade Policy, 2009-2014. The Foreign Trade Policy 2009-2014 (FTP), incorporating provisions relating to export and import of goods and services.
- The Foreign Trade Policy prohibits export or import by any person without an IEC number unless specifically exempted. An IEC number is granted on application by competent authority in accordance with specified procedure.
- Under MAI scheme, financial assistance is provided for export promotion activities on focus country, focus product basis. Financial assistance is also available for Export Promotion Councils (EPCs), Industry and Trade Associations (ITAs), Agencies of State Government, Indian Commercial Missions (ICMs) abroad and other national level institutions/eligible entities.
- Under MDA Scheme, financial assistance is provided for a range of export promotion activities implemented by Export Promotion Councils and Trade Promotion Organizations on the basis of approved annual action plans..
- Merchant as well as Manufacturer Exporters, Service Providers, Export Oriented Units (EOUs) and Units located in Special Economic Zones (SEZs), Agri Export Zones (AEZs), Electronic Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio- Technology Parks (BTPs) shall be eligible for status of export and trading houses.
- Objective of focus market scheme is to offset high freight cost and other externalities to select international markets with a view to enhance India's export competitiveness in these countries. Exporters of all products to notified countries shall be entitled for Duty Credit Scrip.
- Objective of focus product scheme is to incentivise export of such products which have high export intensity/employment potential, so as to offset infrastructure inefficiencies and other associated costs involved in marketing of these products.
- Units undertaking to export their entire production of goods and services (except permissible sales in DTA), may be set up under the Export Oriented Unit (EOU) Scheme, Electronics Hardware Technology Park (EHTP) Scheme, Software Technology Park (STP) Scheme or Bio-Technology Park (BTP) Scheme for manufacture of goods, including repair, re-making, reconditioning, reengineering and rendering of services.

## **SELF TEST QUESTIONS**

1. What are the objectives of foreign trade policy?
  2. Specify the authority responsible for the administration and execution of the FTP?
  3. What do you mean by IEC Number?
  4. Distinguish between Market Access Scheme and Market development Assistance.
  5. Write short notes on:
    - Board of Trade
    - Star Export House



# FOREIGN TRADE POLICY AND PROCEDURE (SPECIAL ECONOMIC ZONES ACT, 2005)

## Section II

### LESSON OUTLINE

- Objective of SEZ Act, 2005
- Salient Features of the SEZ Act, 2005
- Developers
- Infrastructure Facilities
- International Financial Service Centre
- Import
- Export
- Establishment of SEZ
- Guidelines for notifying SEZ
- Board of Approval
- Development Commissioner
- Setting of Unit
- Offshore Banking Unit
- SEZ Authority
- Powers of Central Government to supersede Authority
- Power of the State Government
- Identity Card
- Appeal to high Court
- Reference of dispute
- Offence by companies

### LEARNING OBJECTIVES

Special Economic Zones (SEZ) are growth engines that can boost manufacturing, augment exports and generate employment. The SEZs require special fiscal and regulatory regime in order to impart a hassle free operational regime encompassing the state of the art infrastructure and support services.

Special Economic Zone (SEZ) is a specifically delineated duty free enclave and shall be deemed to be foreign territory for the purposes of trade operations and duties and tariffs. Goods and services going into the SEZ area from Domestic Tariff Area treated as exports and goods coming from the SEZ area into DTA treated as if these are being imported. SEZ units may be set up for manufacture of goods and rendering of services.

The Government of India had announced a Special Economic Zone scheme in April, 2000 with a view to provide an internationally competitive environment for exports. To instil confidence in investors and signal the Government's commitment to a stable SEZ policy regime and with a view to impart stability to the SEZ regime thereby generating greater economic activity and employment through the establishment of SEZs, the Special Economic Zones Act, 2005, was passed by Parliament in 2005.

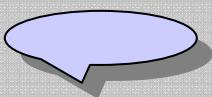
This section deals with how Special Economic Zones Act provides single window approval mechanism, establishment of Authority, Off-Shore Banking Units and Special Court for Special Economic Zones.

SEZ Act, 2005 to provide for the establishment, development and management of the Special Economic Zones for the promotion of exports and for matters connected therewith or incidental thereto.

## INTRODUCTION

While the policy relating to the Special Economic Zones is contained in the Foreign Trade Policy, incentives and other facilities offered to the Special Economic Zone developer and units are implemented through various notifications and circulars issued by the concerned Ministries/Departments. The system, therefore, did not lend enough confidence for investors to commit substantial funds for development of infrastructure and for setting up of the units in the Zones for export of goods and services. In order to give a long term and stable policy framework with minimum regulatory regime and to provide expeditious and single window clearance mechanism, the Government enacted Special Economic Zones Act, 2005.

***The salient features of the Act are as under:—***



- (i) *matters relating to establishment of Special Economic Zone and for setting up of units therein, including requirements, obligations and entitlements;*
- (ii) *matters relating to requirements for setting up of off-shore banking units and units in International Financial Service Center in Special Economic Zone, including fiscal regime governing the operation of such units;*
- (iii) *the fiscal regime for developers of Special Economic Zones and units set up therein;*
- (iv) *single window clearance mechanism at the Zone level;*
- (v) *establishment of an Authority for each Special Economic Zone set up by the Central Government to impart greater administrative autonomy; and*
- (vi) *designation of special courts and single enforcement agency to ensure speedy trial and investigation of notified offences committed in Special Economic Zones.*

## Definitions

Section 2 of the Act contains definitions of the terms used in the Act.

- **“Co-Developer”** means a person who, or a State Government which, has been granted by the Central Government a letter of approval under sub-section (12) of Section 3. [Section 2(f)]
- **“Developer”** means a person who, or a State Government which, has been granted by the Central Government a letter of approval under sub-section (10) of Section 3 and includes an Authority and a Co-Developer. [Section 2(g)]
- **“Export” means—**
  - (i) taking goods, or providing services, out of India, from a Special Economic Zone, by land, sea or air or by any other mode, whether physical or otherwise; or
  - (ii) supplying goods, or providing services, from the Domestic Tariff Area to a Unit or Developer; or
  - (iii) supplying goods, or providing services, from one Unit to another Unit or Developer, in the same or different Special Economic Zone. [Section 2(m)]

➤ ***"Import"* means—**

(i) bringing goods or receiving services, in a Special Economic Zone, by a Unit or Developer from a place outside India by land, sea or air or by any other mode, whether physical or otherwise; or

(ii) receiving goods, or services by a Unit or Developer from another Unit or Developer of the same Special Economic Zone or a different Special Economic Zone. [Section 2(o)]

➤ ***"Infrastructure facilities"* means industrial, commercial or social infrastructure or other facilities necessary for the development of a Special Economic Zone or such other facilities which may be prescribed. [Section 2(p)]**➤ ***"International Financial Services Centre"* means an International Financial Services Centre which has been approved by the Central Government under sub-section (1) of Section 18. [Section 2(q)]**➤ ***"Manufacture"* means to make, produce, fabricate, assemble, process or bring into existence, by hand or by machine, a new product having a distinctive name, character or use and shall include processes such as refrigeration, cutting, polishing, blending, repair, remaking, re-engineering and includes agriculture, aquaculture, animal husbandry, floriculture, horticulture, pisciculture, poultry, sericulture, viticulture and mining. [Section 2(r)]**➤ ***"Offshore Banking Unit"* means a branch of a bank located in a Special Economic Zone and which has obtained the permission under clause (a) of sub-section (1) of Section 23 of the Banking Regulation Act, 1949. [Section 2(u)]**➤ ***"person"* includes an individual, whether resident in India or outside India, a Hindu undivided family, co-operative society, a company, whether incorporated in India or outside India, a firm, proprietary concern, or an association of persons or body of individuals, whether incorporated or not, local authority and any agency, office or branch owned or controlled by such individual, Hindu undivided family, co-operative, association, body, authority or company. [Section 2(v)]**➤ ***"Services"* means such tradable services which.—**

(i) are covered under the General Agreement on Trade in Services annexed as IB to the Agreement establishing the World Trade Organisation concluded at Marrakesh on the 15th day of April, 1994;

(ii) may be prescribed by the Central Government for the purposes of this Act; and

(iii) earn foreign exchange. [Section 2(z)]

### What is Special Economic Zone?

*Special Economic Zone (SEZ) is a specifically delineated duty free enclave and shall be deemed to be foreign territory for the purposes of trade operations and duties and tariffs.*



### Establishment of Special Economic Zone

Section 3 of the Act provides that the Central Government, State Government, or any other person, jointly or severally, may establish a Special Economic Zone. Any person who, intends to set up a Special Economic Zone, may, after identifying the area, make a proposal to the State Government concerned for the purposes of setting up a Special Economic Zone. It also allows a person, at his option to make a proposal directly to

the Board for the purpose of setting up Special Economic Zone. In cases where such proposal has been received directly from a person, the Board may grant approval and after receipt of such approval, the person concerned, is required to obtain the concurrence of the State Government within prescribed time.

In a case a State Government intends to set up the Special Economic Zone, it may after identifying the area, forward the proposal directly to the Board of Approval for setting up of Special Economic Zone. However, the Central Government has been empowered to set up and notify the Special Economic Zone without consulting the State Government concerned; without referring the proposal to the Board.

The State Government may, on receipt of the proposal for setting up a Special Economic Zone forward the proposal together with its recommendations to the Board of Approval within the specified time. The Board of Approval may, after receipt of the proposal for setting up a Special Economic Zone either approve the proposal or, approve the proposal subject to such terms and conditions as it may deem fit to impose. It can also modify or reject the proposal for setting up a Special Economic Zone.

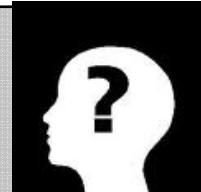
The Central Government has been empowered to specify the minimum area of land for setting up a Special Economic Zone and other terms and conditions subject to which the Board may approve, modify or reject any such proposal received by it. Section 3(9) further provides that if the Board approves the proposal without any modification, it shall communicate the same to the Central Government. If it approves the proposal with modification, it shall, communicate the same to the person or the State Government concerned if the modifications are accepted by the person or State Government, the Board of Approval shall communicate the approval to the Central Government. If it rejects the proposal, it shall record the reasons therefor and communicate the rejection to the person or the State Government concerned.

Section 3(10) requires the Central Government to grant on receipt of communication from the Board of Approval, a letter of approval on such terms and conditions and obligations and entitlements, as approved by Board of Approval, to the person or the State Government concerned. However the Central Government may, on the basis of approval of the Board, approve more than one developer in one Special Economic Zone in cases where one Developer does not have in his possession the minimum area of contiguous land, as may be prescribed, for setting up a Special Economic Zone. In all such cases, each Developer is considered as a Developer in respect of the land in his possession.

This section also provides that any person or a State Government, who intends to provide any infrastructure facilities in the identified area or undertaken any authorised operations may, after entering into an agreement with the Developer, make a proposal for the same to the Board of Approval, for its approval. Every such person or State Government, whose proposal has been approved by the Board and who, or which, has been granted letter of approval by the Central Government, shall be considered a Co-Developer of the Special Economic Zone.

### **Who can set up SEZs?**

*Any private/public/joint sector or State Government or its agencies can set up Special Economic Zone (SEZ)*



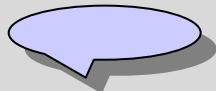
### **Establishment, Approval and Authorization to Operate Special Economic Zone**

Section 4 of the SEZ Act requires the Developer to submit, after the grant of letter of approval, the exact particulars of the identified area to the Central Government which after satisfying that the specified requirements are fulfilled, notify the specifically identified area in the State as a Special Economic Zone.

However, the Central Government has been empowered to notify any additional area as a part of a Special Economic Zone. This section empowers the Central Government to authorise the Developer to undertake such operations in a Special Economic Zone, as it may prescribe.

### Guidelines for notifying Special Economic Zone

***Section 5 stipulates broader guidelines to be considered by the Central Government, while notifying any area as a Special Economic Zone or an area to be included in the SEZ and in discharging its functions under the Act. These include:***



- (a) generation of additional economic activity;
- (b) promotion of exports of goods and services;
- (c) promotion of investment from domestic and foreign sources;
- (d) creation of employment opportunities;
- (e) development of infrastructure facilities; and
- (f) maintenance of sovereignty and integrity of India, the security of the State and friendly relations with foreign States

### The Processing and Non-Processing areas

Section 6 empowers the Central Government or any specified authority to demarcate the areas falling within the Special Economic Zones as -

- (a) the processing area for setting up Units for activities, being the manufacture of goods, or rendering of services;
- (b) the area exclusively for trading or warehousing purposes; or
- (c) the non-processing areas for activities other than those specified under (a) or (b) above.

### Exemption from taxes, duties or cess

Section 7 exempts all goods or services exported out of, or imported into, or procured from the Domestic Tariff Area, by a Unit or Developer in a Special Economic Zone from the payment of taxes, duties or cess under all enactments specified in the First Schedule. The enactments specified in the First Schedule generally relate to levy and payment of cess.

### Constitution of Board of Approval

Section 8 empowers the Central Government to constitute, by notification, the Board of Approval within fifteen days of the commencement of the Act. This section also provides for composition of Board, term of office of Members, co-option of certain persons as Members of the Board, its meetings and quorum, etc.

### Duties, powers and functions of Board of Approval

Section 9 casts upon the Board the duty to promote and ensure orderly development of the Special Economic Zones. The powers and functions of the Board, *inter alia*, include

- (a) granting of approval or rejecting proposal or modifying such proposals for establishment of the Special Economic Zones;

- (b) granting approval of authorised operations to be carried out in the Special Economic Zones by the Developer;
- (c) granting of approval to the Developers or Units (other than the Developers or the Units which are exempt from obtaining approval under any law or by the Central Government) for foreign collaborations and foreign direct investments (including investments by a person resident outside India) in the Special Economic Zone for its development, operation and maintenance;
- (d) granting of approval or rejecting proposal for providing infrastructure facilities in a Special Economic Zone or modifying such proposals;
- (e) granting, a licence to an industrial undertaking referred to in section 3(d) of IDR Act, if such undertaking is established, as a whole or part thereof, or proposed to be established, in a Special Economic Zone;
- (f) suspension of the letter of approval granted to a Developer and appointment of an Administrator under Section 10(1) of the Act;
- (g) disposing of appeals preferred under Section 15(4) and Section 16(4) of the Act;
- (h) performing such other functions as may be assigned to it by the Central Government.

Section 9(3) empowers the Board of Approval to delegate such powers and functions as it may deem fit to one or more Development Commissioners for effective and proper discharge of the functions of the Board. Section 9(5) stipulates that the Board in exercise of its powers and performance of its functions be bound by such directions on questions of policy, as the Central Government may give in writing to it from time to time.

### **Suspension of letter of approval and transfer of Special Economic Zone in certain cases**

Section 10 empowers the Board to suspend the letter of approval granted to the Developer for a whole or part of his area established as Special Economic Zone for a period not exceeding one year and appoint an Administrator to discharge the functions of the developer in accordance with the terms and conditions of the letter of approval and manage the Special Economic Zone accordingly. The suspension may be ordered by the Board, if in its opinion following circumstances exist:

- (i) the developer is unable to discharge the functions or perform the duties imposed on him; or
- (ii) the developer has persistently defaulted in complying with the directions of the Board; or
- (iii) the developer has violated the terms and conditions of the letter; or
- (iv) the financial position of the developer is such that he is unable to fully and efficiently discharge the duties and obligations imposed on him by the letter of approval.

However, no letter of approval can be suspended unless the Board has given to the Developer not less than three months' notice, in writing, stating the grounds on which it proposes to suspend the letter of approval, and has considered any cause shown by the Developer within the period of that notice, against the proposed suspension.

It has been further provided that the Board may, instead of suspending the letter of approval permit it to remain in force subject to such further terms and conditions as it thinks fit to impose. Section 10(4) makes any further terms or conditions so imposed binding upon the Developer. These terms and conditions have the force and effect as if they were contained in the letter of approval.

In case the Board suspends a letter of approval, it has been put under obligation to serve a notice of suspension upon the Developer and fix a date for suspension to take effect. Upon suspension of the letter of

approval, the Special Economic Zone of the Developer vests in the Administrator for a period not exceeding one year or up to the date on which the letter of approval for such Special Economic Zone is transferred, whichever is earlier. This section also contains provisions for transfer of the Special Economic Zone of a Developer whose licence has been suspended and take other actions consequent upon the suspension of the letter of approval. The Board of Approval has been empowered to issue such directions or formulate such scheme as it may consider necessary for operation of such Special Economic Zone.

### **Development Commissioner**

Section 11 empowers the Central Government to appoint the Development Commissioner for one or more Special Economic Zones and such Officers and other employees as it considers necessary to assist every Development Commissioner. It also contains provisions for salary and allowances and other terms and conditions of service in respect of leave, pension, provident fund and other matters of the Development Commissioner, officers and other employees.

### **Functions of the Development Commissioner**

Section 12 dealing with the functions of the Development Commissioner requires every Development Commissioner to take steps in order to discharge his functions to ensure speedy development of the Special Economic Zone and promotion of exports therefrom.

#### ***The functions of the Development Commissioner include :***



- (a) *guide the entrepreneurs for setting up of Units in the Special Economic Zone;*
- (b) *ensure and take suitable steps for effective promotion of exports from the Special Economic Zone;*
- (c) *ensure proper coordination with the Central Government or State Government Departments concerned or agencies with respect to, or for above purposes;*
- (d) *monitor the performance of the Developer and the Units in SEZ;*
- (e) *discharge such other functions as may be assigned to him by the Central Government under this Act or any other law for the time being in force; and*
- (f) *any other functions as may be delegated to him by the Board of approval.*

This section entitles the Development Commissioner to be overall in charge of the Special Economic Zone and to exercise administrative control and supervision over the officers and employees. Every Development Commissioner is also required to discharge such functions and exercise such powers as may be delegated to him by a general or special order by the Central Government or the State Government concerned, as the case may be. The section further empowers the Development Commissioner to call for such information from a Developer or Unit from time to time as may be necessary to monitor the performance of the Developer and the Unit. The Development Commissioner has been authorised to delegate any or all of his powers or functions to any of the officers employed under him.

### **Constitution of Approval Committee**

Section 13 empowers the Central Government to constitute by notification, a Committee for every Special Economic Zone, to be called the Approval Committee to exercise the powers and perform the functions as

specified. In the case of existing Special Economic Zones, the Approval Committee is required to be constituted within six months from the date of commencement of the Act and in case of other Special Economic Zones established after the commencement of the Act within six months from the date of establishment of such Special Economic Zone. This section also contains provisions relating to composition of meetings and its quorum and requires all orders and decisions and instructions of the Approval Committee to be authenticated by the signature of the Chairperson or any other Member as may be authorised by the Approval Committee.

### **Powers and Functions of Approval Committee**

Section 14 empowers every Approval Committee to discharge the functions and exercise the powers in respect of the following matters:

- (a) approve, the import or procurement of goods from the Domestic Tariff Area, for carrying on the authorised operations by a Developer in the Special Economic Zone;
- (b) approve providing of services by a service provider from outside India or from the Domestic Tariff Area for carrying on the authorised operations by the Developer, in the Special Economic Zone;
- (c) monitor the utilisation of goods or services or warehousing or trading in the Special Economic Zone;
- (d) approve, modify or reject proposals for setting up Units for manufacturing or rendering of services or warehousing or trading in SEZ in accordance with the provisions of Section 15(8) of the Act;
- (e) allow on receipt of approval foreign collaborations and foreign direct investments, including investments by a person outside India for setting up a Unit;
- (f) monitor and supervise compliance of conditions subject to which the letter of approval or permission, if any, is granted to the Developer or entrepreneur; and
- (g) perform any other functions as may be entrusted to it by the Central Government or the State Government concerned, as the case may be.

In case the developer is Central Government, the approval committee has been empowered to exercise all powers of the approval committee, until the constitution of Approval Committee.

### **Setting up of Unit**

Section 15 entitles any person, who intends to set up a Unit for carrying on the authorised operations in a Special Economic Zone, to submit a proposal to the Development Commissioner concerned. The Development Commissioner in turn place the proposal before the Approval Committee for its approval. The Approval Committee may, approve the proposal with or without modification, and subject to such terms and conditions as it may deem fit, or reject the same. In case of modification or rejection of a proposal, the Approval Committee has been put under obligation to afford a reasonable opportunity of being heard to the person concerned and after recording the reasons therefor, either modify or reject the proposal. Sub-section (4) entitles a person aggrieved by an order of the Approval Committee, to make an appeal to the Board of Approvals, within the prescribed time and specified manner. Sub-section (8) empowers the Central Government to prescribe the requirements (including the period for which a unit may be set up) subject to which the Approval Committee may approve, modify or reject the proposal. The Development Commissioner may, after the approval of the proposal, grant a letter of approval to the person concerned to set up a Unit and undertake in the Unit such operations which the Development Commissioner may authorise and every such operation so authorised is mentioned in the letter of approval.

### **Cancellation of letter of approval granted to entrepreneur**

Section 16 empowers the Approval Committee to cancel the letter of approval of an entrepreneur after reasonable opportunity of being heard has been afforded to the entrepreneur. The Approval Committee may,

at any time, cancel the letter of approval if it has any reason or cause to believe that the entrepreneur has persistently contravened any of the terms and conditions or its obligation subject to which the letter of approval was granted to the entrepreneur. It further provides that where the letter of approval has been cancelled, the Unit shall not, from the date of such cancellation, be entitled to any exemption, concession, benefit or deduction available to it as such and such Unit shall remit the exemption, concession, drawback and any other benefit availed by the entrepreneur in respect of the capital goods, finished goods lying in the stock and unutilised raw materials in the prescribed manner. Sub-section (4) entitles any person aggrieved from an order of the Approval Committee to make an appeal to the Board of Approval within the prescribed time.

### **Setting up and operation of Offshore Banking Unit**

Section 17 dealing with setting up and operation of offshore Banking Unit provides that an application for setting up and operation of an Offshore Banking Unit in a Special Economic Zone may be made to the Reserve Bank, in the prescribed form and manner. The Reserve Bank, of India may, on being satisfied that the applicant fulfills all the specified conditions, grant permission to such applicant for setting up and operation of an Offshore Banking Unit in a Special Economic Zone. Sub-section (3) empowers the Reserve Bank to specify, by notification, the terms and conditions subject to which an Offshore Banking Unit may be set up and operated in the Special Economic Zone.

#### **What do you mean by Offshore Banking Unit?**

*"Offshore Banking Unit" means a branch of a bank located in a Special Economic Zone and which has obtained the permission under clause (a) of sub-section (1) of Section 23 of the Banking Regulation Act, 1949.*



### **Setting up of International Financial Services Centre**

Section 18 empowers the Central Government to approve setting up of an International Financial Services Centre in a Special Economic Zone and to specify requirements for setting up the operation of such Centre. However, the Central Government may approve only one international Financial Services Centre in a Special Economic Zone. The Central Government may subject to the guidelines as may be framed by the Reserve Bank, the Security and Exchange Board of India, the Insurance Regulatory and Development Authority and such other authority as it may deem fit, prescribe the requirement for setting up and terms and conditions of the operation of International Financial Services Center.

#### **Single application form, return, etc.**

Section 19 empowers the Central Government to prescribe single application form for obtaining any licence, permission or registration or approval by a Developer or an entrepreneur under one or more Central Acts. Section 19(b) empowers the Central Government to authorise the Board, the Development Commissioner and the approval Committee to exercise its powers on matters relating to the development of SEZ or setting up or operation of units. Section 19(c) empowers the Central Government to prescribe single form for furnishing returns or information by a developer or an entrepreneur under one or more Central Acts.

#### **Agency to inspect**

Section 20 empowers the Central Government to specify, by notification, any officer or agency for carrying out surveys or inspections for securing the compliance with the provisions of any Central Act by a Developer or an entrepreneur, as the case may be, and such officer or agency is required to submit verification or compliance report, in such manner and within such time as may be specified in the said notification.

### **Single enforcement officer or agency for notified offences**

Section 21 empowers the Central Government to specify by notification, any act or omission made punishable under any Central Act, as notified offence for purposes of the proposed legislation. It further empowers the Central Government to authorise any officer or agency to be the enforcement officer or agency in respect of any notified offence committed in a Special Economic Zone. Every officer or agency so authorised has been granted all the corresponding powers of investigation, inspection, search or seizure as provided under the relevant Central Act in respect of the notified offences.

### **Investigation, Inspection, Search or Seizure**

Section 22 empowers the agency or officer, with prior intimation to the Development Commissioner concerned to carry out the investigation, inspection, search or seizure in the Special Economic Zone or in a Unit if such agency or officer has reason to believe (reasons to be recorded in writing) that a notified offence has been committed or is likely to be committed in the Special Economic Zone. However, no investigation, inspection, search or seizure is allowed to be carried out in a SEZ by any agency or officer other than those referred to in Section 21(2) or (3), without prior intimation or approval of the concerned Development Commissioner. It is further provided that an officer or agency, if so authorised by the Central Government, may carry out the investigation, inspection, search or seizure in the Special Economic Zone or Unit without prior intimation or approval of the Development Commissioner.

### **Designated Courts to try suits and notified offences**

Section 23 empowers the concerned State Government, in which SEZ is situated, to designate, with the concurrence of the Chief Justice of the High Court of that State, one or more Courts to try all suits of a civil nature arising out of offences committed in the Special Economic Zone. Section 23(2) provides that no court, other than the designated court shall try any suit or conduct the trial of any notified offence.

### **Appeal to High Court**

Section 24 entitles any person aggrieved by any decision or order of the designated Court to file an appeal to the High Court within sixty days from the date of communication of the decision or order of the said court to him on any question of fact or law arising out of such orders. However the High Court can, if it is satisfied that the appellant was prevented by sufficient cause from filing an appeal within the prescribed period of sixty days allow it to be filed within a further period not exceeding sixty days.

### **Offences by Companies**

Section 25 dealing with offences by companies provides that where an offence has been committed by a company, every person who at the time the offence was committed was in charge of and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. However such person shall not be liable to any punishment if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence.

Section 25(2) provides that where an offence has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall, also be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

### **Exemptions, drawbacks and concessions to every Developer and entrepreneur**

Section 26 contains provisions relating to exemptions, drawbacks and concessions to Developer and entrepreneur from any duty of customs under the Customs Act, 1962, the Customs Tariff Act, 1975, the Central Excise Act, 1944 or the Central Excise Tariff Act, 1985 or any other law for the time being in force, exemption from the service tax under Chapter V of the Finance Act, 1994 and exemption from levy of taxes on sale or purchase of goods other than newspapers under the Central Sales Tax Act, 1956 if such goods are meant to carrying on authorised operations by the developer or entrepreneur. The developer or entrepreneur has also been entitled to drawback or such other benefits as may be admissible from time to time on goods brought or services provided from DTA into SEZ or unit or services provided in SEZ or unit by service providers located outside India to carry on the authorised operations by the Developer or entrepreneur. The Central Government has also been empowered to specify the manner in which and the terms and conditions subject to which, the exemptions, concessions, drawbacks or other benefits are to be granted to developer or entrepreneur.

### **Application of the provisions of the Income Tax Act, 1961 with certain modifications in relation to Developers and entrepreneurs**

Section 27 provides for application of the provisions of the Income Tax Act, 1961 to the Developer and entrepreneur for carrying on the authorised operations in the Special Economic Zones or Unit subject to modifications specified in the second schedule.

### **Duration of goods & services in Special Economic Zones**

Section 28 empowers the Central Government to specify, the period during which any goods brought into, or services provided in, any Unit or Special Economic Zone without payment of taxes, duties, levies or cess, shall remain or continue to be provided in such Unit or Special Economic Zone.

### **Transfer of ownership and removal of goods**

Section 29 allows the transfer of ownership in any goods brought into, or produced or manufactured in, any Unit or Special Economic Zone or removal thereof from such Unit or Zone, subject to such terms and conditions as specified by the Central Government.

### **Domestic clearance by Units**

Section 30 provides that any goods removed from a Special Economic Zone to the Domestic Tariff Area be chargeable to duties of customs including anti-dumping, countervailing and safeguard duties under the Customs Tariff Act, 1975, where applicable, as leviable on such goods when imported. This section further provides that the rate of duty and tariff valuation, if any, applicable to goods removed from a Special Economic Zone shall be at the rate and tariff valuation in force as on the date of such removal, and where such date is not ascertainable, on the date of payment of duty. This section empowers the Central Government to make rules specifying conditions in this regard.

### **Special Economic Zone Authority**

Section 31 dealing with the Constitution of Authority empowers the Central Government to constitute by notification in the Official Gazette, an Authority for every SEZ to exercise powers conferred on and discharge the functions assigned to it.

In the case of an existing SEZ established by the Central Government the Central Government has been empowered to establish such authority within six months from the date of commencement of the Act. It is

further provided that the person or authority (including Development Commissioner) which is exercising control over an existing SEZ, shall continue to do so till the authority is constituted. Section 31(2) provides that every authority shall be a body corporate by name as assigned, having perpetual succession and a common seal, with power to acquire, hold and dispose of property, both movable and immovable and to contract and shall sue and be sued. Section 31(9) stipulated that no act or proceedings of an authority shall be invalidated merely by reason of:

- (i) any vacancy in or any defect;
- (ii) any defect in the appointment of a person as its member; or
- (iii) any irregularity in the procedure of the authority not affecting the merits of the case.

### **Functions of Authority**

Section 34 casts upon the Authority a duty to undertake such measures as it thinks fit for the development, operation and management of the respective Special Economic Zone. Section 34(2) provides for following measures :

- (a) the development of infrastructure in the Special Economic Zone;
- (b) promoting exports from the Special Economic Zone;
- (c) reviewing the functioning and performance of the Special Economic Zone;
- (d) levy user or service charges or fees or rent for the use of properties belonging to the Authority;
- (e) performing such other functions as may be prescribed.

### **Directions by the Central Government**

Section 38 empowers the Central Government to give directions to the authority and makes it binding for every Authority of the Special Economic Zone to carry out the directions issued from time to time in this regard.

### **Returns and reports by the Authority**

Section 39 casts upon every Authority of the Special Economic Zone a duty to furnish to the Central Government such returns and statements and such particulars in regard to the promotion and development of exports and the operation and maintenance of the Special Economic Zone and Units as it may require from time to time. This section further requires every authority to submit to the Central Government after the end of each financial year a report in form and before specified date, giving a true and full account of its activities, policy and programmes during the previous financial year. Section 39(3) requires a copy of every such report to be laid before each House of Parliament, soon after its receipt

### **Power of the Central Government to Supersede Authority**

Section 40 empowers the Central Government to supersede an Authority for a maximum period of six months if at any time it is of the opinion that an Authority is unable to perform, or has persistently made default in the performance of the duty imposed on it or has exceeded or abused its powers, or has wilfully or without sufficient cause, failed to comply with any direction issued by it. However, before issuing a notification superseding an authority, the Central Government is required to give reasonable time to that Authority to make representation against the proposed suppression and consider the representations, if any, of the Authority. Section 40(2) dealing with the consequences of publication of the notification superseding the Authority, provides that,

- (a) the Chairperson and other Members of the Authority shall, notwithstanding that their term of office has not expired as from the date of supersession, vacate their offices as such;

- (b) all the powers, functions and duties which may, by or under the provisions of the Act, be exercised or discharged by or on behalf of the Authority shall, during the period of supersession, be exercised and performed by such person or persons as the Central Government may direct;
- (c) all property vested in the Authority shall, during the period of supersession, vest in the Central Government.

Section 40(3) also provides that on the expiration of the period of supersession specified in the notification, the Central Government may extend the period of supersession for such further period not exceeding six months or reconstitute the Authority in the prescribed manner.

### Reference of Dispute and Limitation

Section 42 requires any dispute of civil nature arising among two or more entrepreneurs or two or more Developers or between the entrepreneur and Developer in the Special Economic Zone to be referred to arbitration provided, the court or the courts to try suits in respect of such dispute had not been designated. However no dispute should be referred to the arbitration on or after the date of the designation of court or courts under section 23(1). It further provides that where a dispute has been referred to arbitration, the same shall be settled or decided by the arbitrator to be appointed by the Central Government and the provisions of the Arbitration and Conciliation Act, 1996 shall apply to all arbitrations.

Section 43 stipulates that the period of limitation in the case of any dispute which is required to be referred to arbitration shall be regulated by the provisions of the Limitation Act, 1963, as if the dispute was a suit and the arbitrator is civil court. Section 43(2), however, empowers the arbitrator to admit, a dispute after the expiry of the period of limitation, if the arbitrator is satisfied that the applicant had sufficient cause for not referring the dispute within specified period.

### Person to whom a communication to be sent

Section 45 provides that a communication by any competent authority or person may be sent to the person who has the ultimate control over the affairs of the Special Economic Zone or Unit or where the said affairs are entrusted to a manager, director, chairperson, or managing director, or to any other officer, by whatever name called, such communication may be sent to such manager, director, chairperson, or managing director or any other officer.

### Identity card



*Section 46 requires that every person whether employed or residing or required to be present in a Special Economic Zone be provided an identity card by every Development Commissioner in prescribed form and containing specified particulars.*

### Power of the Central Government to modify provisions of the Act or other enactments in relation to Special Economic Zones

Section 49 empowers the Central Government to direct, by notification in the Official Gazette, that any of the provision of the Act or any other Central Act, any rules or regulations made thereunder or any notification or order issued or direction given thereunder specified in the notification shall not apply to a Special Economic Zone or a class of Special Economic Zones or all Special Economic Zones; or shall apply to a Special Economic Zone or a class of Special Economic Zones or all Special Economic Zones only with such exceptions, modification and adaptation, as may be specified in the notification. Sub section (2) requires a copy of every notification proposed to be issued to be laid in draft before each House of Parliament. The

notification shall not be issued or, as the case may be, shall be issued only in such modified form as may be agreed upon by both the Houses of Parliament.

### **Power of State Government to grant exemption**

Section 50 empowers the State Government to notify policies for Developers and Units and to take suitable steps for enactment of any law -

- (a) granting exemption from the State taxes, levies and duties to the Developer or the entrepreneur;
- (b) delegating the powers conferred upon any person or authority under any State Act to the Development Commissioner in relation to the Developer or the entrepreneur.

### **SEZ Act to have overriding effect**



*Section 51 giving overriding effect to this Act provides that 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.*

### **Special Economic Zones to be ports, airports inland container depots, land stations etc. in certain cases**

Section 53 provides that a Special Economic Zone, on and from the appointed day, be deemed to be a territory outside the customs territory of India for the purposes of undertaking the authorised operations. This section further provides that a Special Economic Zone shall, with effect from such date as the Central Government may notify, be deemed to be a port, airport, inland container depot, land station and land customs stations under section 7 of the Customs Act, 1962. The Central Government has been empowered to notify different dates for different Special Economic Zones.

### **Special Economic Zones Rules, 2006**

Section 55 empowers the Central Government to make rules in respect of specified matters and requires that the same be published in the Official Gazette and be laid before each House of Parliament. In this context, the Central Government has notified the Special Economic Zones Rules, 2006 on February 10, 2006.

### **LESSON ROUND UP**

- Special Economic Zones (SEZ) are growth engines that can boost manufacturing, augment exports and generate employment. The SEZs require special fiscal and regulatory regime in order to impart a hassle free operational regime encompassing the state of the art infrastructure and support services.
- Special Economic Zone (SEZ) is a specifically delineated duty free enclave and is deemed to be foreign territory for the purposes of trade operations and duties and tariffs.
- SEZ units are governed by Special Economic Zones Act, 2005.
- Central Government, State Government, or any other person, jointly or severally, may establish a Special Economic Zone. Any person who, intends to set up a Special Economic Zone, may, after identifying the area, make a proposal to the State Government concerned for the purposes of setting up a Special Economic Zone.
- Board of Approval granting of approval or rejecting proposal or modifying such proposals for establishment of the Special Economic Zones.

- Every Development Commissioner to take steps in order to discharge his functions to ensure speedy development of the Special Economic Zone and promotion of exports there from.
  - The Central Government to constitute by notification, a Committee for every Special Economic Zone, to be called the Approval Committee to exercise the powers and perform the functions as specified.
  - Any person, who intends to set up a Unit for carrying on the authorised operations in a Special Economic Zone, to submit a proposal to the Development Commissioner concerned.
  - An application for setting up and operation of an Offshore Banking Unit in a Special Economic Zone may be made to the Reserve Bank of India.
  - SEZ Act casts upon the SEZ Authority a duty to undertake such measures as it thinks fit for the development, operation and management of the respective Special Economic Zone.
  - Every person whether employed or residing or required to be present in a Special Economic Zone be provided an identity card by every Development Commissioner in prescribed form and containing specified particulars.
  - Provisions of the SEZ 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.
  - Any person aggrieved by any decision or order of the designated Court to file an appeal to the High Court within sixty days from the date of communication of the decision or order of the said court to him on any question of fact or law arising out of such orders.

## SELF TEST QUESTIONS

1. Special Economic Zones are growth engines. Discuss.
  2. Discuss in detail the salient features of SEZ Act, 2005.
  3. Explain the procedure for establishment of SEZ.
  4. Briefly discuss the duties, powers and functions of Board of Approval in respect of Special Economic Zones.
  5. What are the functions of Approval Committee under SEZ Act, 2005.



# Lesson 3

## COMPETITION AND CONSUMER PROTECTION

### (THE COMPETITION ACT, 2002)

### Section I

#### LESSON OUTLINE

- Competition and Economic efficiency
- Competition Law and Policy
- Competition Regime in India
- Anti-Competitive Agreement
- Abuse of Dominant Position
- Combination
- Regulation of Combination
- Director General
- Enquiry into certain agreements and dominant position of enterprise
- Enquiry into Combination by Commission
- Competition Commission of India
- Competition Appellate Tribunal (CAT)
- Competition Advocacy
- Offences and penalties
- Power of the Central Government to make Rules
- Appeal to CAT
- Appeal to Supreme Court

#### LEARNING OBJECTIVES

Competition refers to a situation in a market place in which firms/ entities or sellers independently strive for the patronage of buyers in order to achieve a particular business objective, such as profits, sales, market share etc. Competition is not an end unto itself, rather a means to achieve economic efficiency and welfare objectives. Free and fair competition is one of the pillars of an efficient market economy. Therefore, competition has become a driving force in the global economy.

Indian economy is on a high growth path. In the recent years the Indian economy has been one of the strongest performers in the world. However, the full growth potential of the economy remains yet to be realised. Infusion of greater degree of competition can play a catalytic role in unlocking the fuller growth potential in many critical areas of the economy, which hitherto has been held back by restriction on competition in various forms.

This section deals with the Competition Act, 2002 covers anti-competitive agreements, abuse of dominance, Combination, competition Advocacy, Competition Commission of India, Competition Appellate Tribunal and Role of professional under Competition Act, 2002. The Competition Act also covers all commercial activities of Government-related bodies except sovereign functions of the Government.

The Competition Act, 2002 to provide, keeping in view of the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in the markets, to protect the interest of consumers and to ensure freedom of trade carried on by other participant in the markets in India and for matters connected therewith or incidental thereto.

## INTRODUCTION

There is a growing recognition that a flexible, dynamic and competitive private sector is essential to fostering sustained economic development. Promoting effective competition spurs firms to focus on efficiency and improves consumer welfare by offering greater choice of higher-quality products and services at lower prices. It also promotes greater accountability and transparency in government-business relations and decision making, helps reduce corruption, lobbying, and rent seeking. In addition, it provides opportunities for broadly based participation in the economy and for sharing in the benefits of economic growth.

The idea of competition has had, for two centuries or more, a powerful influence on the way we think about our society, the way we organise things and the way we conduct our own economic and personal lives. The competition being an essential element in the efficient working of markets encourages enterprise and efficiency and widens choice. By encouraging efficiency in industry, competition in the domestic market whether between domestic companies alone or between those and overseas companies also contribute to international competitiveness. The full benefits of competition are, however, felt in markets that are open to trade and investment.

Economic theory suggests that prices and quantities in a competitive market equilibrate to levels that generate efficient outcomes at a given point of time. Competition is therefore, beneficial as it provides to consumers wider choice and provides sellers with stronger incentives to minimize costs, so eliminating waste. Competition increases the likelihood that cost savings resulting from efficiency gains will be passed on to a firm's customers, who may be either final consumers or intermediary customers (in which case costs of those firms are also lowered). Ample empirical evidence supports these arguments. The importance of competition for achieving a higher rate of innovation and adoption of new technologies over time is critical for sustaining rapid growth. Yet it is not automatic, and is not the same as *laissez faire*.

In fact, there are reasons to believe that less mature markets tend to be more, rather than less, vulnerable to anti-competitive practices than the markets of developed countries. Reasons include: (a) high "natural" entry barriers due to inadequate business infrastructure, including distribution channels, and (sometimes) intrusive regulatory regimes; (b) asymmetries of information in both product and credit markets; and (c) a greater proportion of local (non-tradable) markets. Competition also serves to diffuse socio-economic power, broadening participation in economic, social, and political advances while ensuring opportunities for new entrepreneurs. Moreover, it can facilitate realization of the benefits for the domestic economy of integrating into international trade and investment patterns.

Several studies have demonstrated the stimulating effects of competitive markets in terms of growth and prosperity. William Lewis in his book, *The Power of Productivity* underlines this point forcefully with his observations on the growth of productivity in the late 1990s in the United States. The author has argued that more than technology and other factors, what matters above all is competition. Similarly, economist Paul London in his book, *The Competition Solution* concludes that heightened competition in the US overshadowed tax cuts or new technologies in explaining the prosperity of the 1990s. Competitive pressures helped suppress inflation and raise living standards through improved productivity. The author noted that competition from imports forced the steel and auto industry, among other manufacturers, to streamline, thereby pushing manufacturing productivity up by 4% a year. Competition has brought down real air fares, telephone rates and several other costs. Where jobs have been lost in one industry, these have been more than compensated by jobs created elsewhere; thus employment has not suffered but has shifted from losers to winners. This argument underlines across the board, the benefits of competition to a wide sections of society, including consumers, workers and many others.

## Definition of Competition

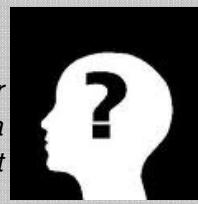
Competition is a complex and technical subject which does not lend itself to easy summary or concise clarification. Of late, with globalisation and opening of the markets worldwide, it has become a subject of great practical importance. It involves the establishment and development of concepts, legal principles and policies for the benefit of consumer interest. The principles and policies are applied to a wide range of private agreements and arrangements, which commercial undertakings enter into for themselves or with each other. In addition, they also apply to the policies and directions of the Government.

In the absence of a generally accepted definition of the phenomenon of competition, it has to be regarded as the object fostered and protected by competition policy and law. The World Bank and OECD in its Report *A Framework for the Design and Implementation of Competition Law and Policy*, broadly defines the competition is “a situation in a market in which firms or sellers independently strive for the buyers’ patronage in order to achieve a particular business objective, for example, profits, sales or market share.”

Competition can also be defined as a process of economic rivalry between market players to attract customers. These market players can be multinational or domestic companies, wholesalers, retailers, or even the neighborhood shopkeeper. In their pursuit to outdo rival enterprises, market players either adopt fair means (producing quality goods, being cost efficient, adopting appropriate technologies, etc.) or indulge in unfair measures (carrying out restrictive business practices – such as predatory pricing, exclusive dealing, tied selling, collusion, cartelisation, abuse of dominant position, etc.). However, in the interest of consumers, and the economy as a whole, it is necessary to promote an environment that facilitates fair competitive outcomes in the market, curb anti-competitive behaviour and discourage market players from adopting unfair measures.

### What is competition in the market?

*In common parlance, competition in the market means sellers striving independently for buyers' patronage to maximize profit (or other business objectives). A buyer prefers to buy a product at a price that maximizes his benefits whereas the seller prefers to sell the product at a price that maximizes his profit.*



## Competition and Economic Efficiency

A number of empirical studies found a positive relationship between competition and innovation, productivity and economic growth. P. Aghion and P. Howitt in *Endogenous Growth Theory* offered several theoretical situations where competition is conducive to innovation – Intensified product market competition could force managers to speed up the adoption of new technologies; Intensive product market competition with incumbent firms engaged in step by step innovative activities could enhance each firms incentive to acquire or increase its technological lead over its rivals and, if labour markets are flexible, competition will induce skilled workers to move to opportunities employing best practices and technologies. Competition also reduces slack by providing more incentives for managers and workers to increase efforts and improve efficiency. Therefore, the product market competition disciplines firms into efficient operation.

Nickel et.al. in his article *Competition and Corporate Performance* suggested three different channels of incentives – competition creates greater opportunities for comparing performance; a more competitive environment where price elasticity of demand tends to be higher, induces greater efforts among workers and managers for cost reducing improvements in productivity since improvements could generate larger increase in revenue and profits; and a more competitive environment forces managers to improve efficiency, because more intense the competition, greater the chances for inefficient to be extinguished.

*UK White Paper on World Class Competition Regime* clearly brings out the importance of competition in an increasingly innovative and globalised economy. Vigorous competition between firms is the lifeblood of strong and effective markets. Competition helps consumers get a good deal. It encourages firms to innovate by reducing slack, putting downward pressure on costs and providing incentives for the efficient organisation of production.

Empirical evidences show that strong competition is closely linked to dynamic and efficient markets. The benefits of competitive forces for economic growth and consumer welfare are widely recognized and evidenced by several studies. Recently, an empirical study in the U.K. by the Centre for Competition Policy, University of East Anglia showed that prices were more than halved through competition in international telephony and airfares, and were significantly reduced in other areas. The survey also brought home the point that competition is not just about prices but is typically multi-faceted, bringing new ways of doing business and leading to technological and other advances.

Michel Porter in his recent work *Can Japan Compete?* shows that in Japan only those sectors characterized by strong domestic competition remain internationally competitive following the country's recent economic downturn, examples include cameras, automobiles and audio equipment. Many leading competition experts believe in the premise that, in the presence of competition, the market will achieve the objective of maximising welfare.

### **Competition Law and Policy**

The World Bank and OECD in its Report *A Framework for the Design and Implementation of Competition Law and Policy* pointed out that a dynamic and competitive environment, underpinned by sound competition law and policy, is an essential characteristic of a successful market economy. Effective enforcement of competition law and active competition advocacy can also be powerful catalysts for successful economic restructuring. This in turn fosters flexibility and mobility of resources, which in the current global business environment are critical elements for the competitiveness of firms and industries across nations. Although the field of competition law and policy is evolving rapidly and includes many different viewpoints on specific issues, recognition is growing that effective competition law is important in shaping business culture and that its proper implementation needs to allow for the education of business people, government officials, the judiciary, and the interested public.



*The basic purpose of Competition Policy and law is to preserve and promote competition as a means of ensuring efficient allocation of resources in an economy. Competition policy typically has two elements: one is a set of policies that enhance competition in local and national markets. The second element is legislation designed to prevent anti-competitive business practices with minimal Government intervention, i.e., a competition law. Competition law by itself cannot produce or ensure competition in the market unless this is facilitated by appropriate Government policies. On the other hand, Government policies without a law to enforce such policies and prevent competition malpractices would also be incomplete.*

Competition policies cover a much broader set of instruments than competition law, and typically include all policies aimed at increasing the intensity of competition or rivalry in local and national markets by lowering entry barriers and opportunities for harmful coordination, to ensure that markets work effectively and serve the interests of all citizens. Competition law is only a subset of a nation's competition policies. Competition policies typically include pro-competition approaches to trade, investment, sectoral regulation, and consumer protection. The barriers to international or interregional trade, restrictions on Foreign Direct Investment (FDI) and technology transfers, restrictions on entry in regulated network utility industries, regulations affecting the

registration of new enterprises and the taxation and corporate governance of existing enterprises, and rules on marketing practices all influence the extent of competitive pressures in markets and so are appropriate concerns of competition policies. In many countries, competition authorities have become the focal point for consultations and putting forward pro-competition viewpoints across a broad range of policy areas.

Asian Development Bank in "During economic transition or reforms", observed that "the benefits of an open market economy cannot be fully realized unless restrictions on competition are removed. Opening markets is not enough by itself for countries to begin reaping the benefits of competition; firms will still find incentives to engage in anti-competitive practices. Thus, the intended benefits of trade reforms may not be realized without active enforcement of competition law. This highlights the importance of having faith in the benefits of competition from an early stage of economic growth and of incorporating competition policy into the broader economic policy framework."

Prof. Paul Geroski, former Chairman, Competition Commission of the United Kingdom observed that "Competition policy is about ensuring that markets are, and remain, competitive. This brings benefits to consumers eventually in all the ways. However, eliminating anti-competitive practices and dismantling monopoly positions that lead to abuses also benefit firms whose business suffers from these practices and abuses. It is worth emphasizing that many of the benefits that emanate from proper application of competition policy are felt in the first instance by firms. This is important for those who seem to think of competition policy as an added and unnecessary burden on business. Competition policy is sometimes a burden on business, but only on those businesses that try to unfairly disadvantage their rivals in ways that reduce their competitive abilities or incentives to compete vigorously".

Hence, competition policy and competition law need to be distinguished. The former can be regarded as a genus, of which, the latter is specie.

## COMPETITION REGIME IN INDIA

### Historical Perspective

The Indian economy remained subject to controls and regulations for several decades, such as industrial licensing, foreign exchange restrictions, small scale industry protection, control on foreign investment and technologies, quantitative restrictions on imports, administered prices, and control on capital issues. The domestic industry was thus insulated from competition.

The economic consequences of this policy regime, though initially beneficial, were reflected in a poor rate of economic growth, low levels of productivity and efficiency, absence of international competitiveness, sub-optimal size of businesses, and outdated and inefficient technologies in various sectors.

India has therefore witnessed two phases of development process with different policy regimes and institutional frameworks. In the first phase, since independence, the transformation and development of the Indian economy took place within a planned, rigidly regulated and relatively closed economic framework. In the second phase, since 1991, when the country embarked upon reform process and embraced market oriented policies.

In the late 1980s and early 1990s, need for liberalization policies was recognized and a range of policy and regulatory reforms were initiated, such as delicensing of industry, shrinking the monopoly of the public sector industries (other than those where strategic and security concerns dominated), removal of quantitative restrictions on imports, market determined exchange rate, liberalization of foreign direct investment, capital market reforms, liberalizing the financial markets, reduction in small scale industry reservations, and a much greater role for the private sector in infrastructure industries such as power, port, transport and communications.

## **Economic Reforms and Competition**

The world economy has been experiencing a progressive international economic integration for the last half a century. There has been a marked acceleration in this process of globalisation and also liberalisation during the last three decades.

Since 1991, the Government of India has introduced a series of economic reforms, including policies of liberalisation, deregulation, disinvestment and privatisation. The seriousness of macroeconomic imbalances and unanimity towards reform rendered this possible. The broad thrust of the new policies was a move away from the centralised allocation of resources in some key sectors by the government to allocation by market forces. Private participation in economic development has emerged as an alternative to the state-oriented development strategy in the reform period.

After a decade of reforms, restraints to competition such as state monopolies and protective measures and controls have been replaced by relatively more competitive and de-regulated open market policies. In the post reform period, the private sector participation in production and supply of utility services has increased substantially. Independent regulators have been established for many sectors such as road, power, telecommunications and insurance. These sectoral regulators have been empowered to determine sector specific entry conditions and eventually the level of competition. In nutshell, post reforms period witnessed an open market orientation in industrial policy, foreign trade policy, foreign investment policy and financial sector policy, infrastructure policy, etc.

## **Competition Law-Evolution and Development**

The first Indian competition law was enacted in 1969 and was christened as the Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act). The genesis of the MRTP Act, 1969 is traceable to Articles 38 and 39 of the Constitution of India. The Directive Principle of State Policy in those Articles lays down, *inter-alia* that the State shall strive to promote the welfare of the people by securing and protecting as effectively, as it may, a social order in which justice - social, economic and political- shall inform all the institutions of the national life, and the State shall, in particular, direct its policy towards securing:

1. that the ownership and control of material resources of the community are so distributed as best to subserve the common good; and
2. that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment.

Legal framework dealing with competition in India spread over other legislations, besides the Monopolies and Restrictive Trade Practices Act, 1969, other legislations dealing with competition include Consumer Protection Act, 1986, the Patents Act 1970 etc.

## **Background to the MRTP Act, 1969**

India, when it became free from the colonial power was industrially very backward. In fact, it inherited an economy in a ravaged condition. Under development of the economy in many respects led the successor Government to adopt a system of planning. In the interest of transformation of the backward industrial economy into an advanced industrial economy, the planners thought it fit to allow the then established industries to develop and grow further. Alongside, mixed economy was also developed as a concept of economic planning. No doubt, there was perceptible growth in industrialisation. However, this also brought on its trails, concentration of wealth and economic power. This led to widening of the difference between the haves and have nots in the society. The Government of India therefore set up the Monopolies Inquiry Commission in 1964 with a view to finding out the causes, the nature and the extent of concentration of economic power in the country and to suggest remedial measures therefor.

The Monopolies Inquiry Commission submitted a detailed report in October 1965 which was well documented and revelatory of many facets of concentration of economic power. Many of the trade practices which were designed to stifle competition in the market and to promote monopolistic tendency were also noticed by the Commission in the course of its inquiry. The Commission observed that there was no need to strike at the concentration of economic power as such but to do so only when it became a menace to the best production in quality and quantity or to fair distribution. Monopolistic conditions in any industrial sphere should be discouraged without injury to the interests of the general public and monopolistic and restrictive trade practices should be curbed except when they were conducive to the common good. The Commission pointed out that on the one hand over the years certain business houses had built vast industrial empires and on the other hand they were trying to accentuate and enlarge the empires by adopting certain trade practices which were intended to distort competition in the market and promote a set of near monopoly conditions. The Commission felt that such tendencies seemed to destroy the basic concept of socio-economic justice enshrined in the Constitution. The Commission also framed a draft Bill as a part of its recommendations.

The Monopolies and Restrictive Trade Practices Bill was introduced in Parliament in 1967 which after being referred to the Joint Select Committee became an Act and finally came into force w.e.f. 1st June, 1970.

The enactment was based on the socio-economic philosophy enshrined in the Directive Principles of State Policy contained in the Constitution which provides that the State shall direct its policy towards securing that the ownership and control of material resources of the community are distributed as best to subserve the common good and that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment.

The principal objectives of the Act, as spelt out in the preamble were:

- (i) prevention of concentration of economic power to the common detriment;
- (ii) control of monopolies;
- (iii) prohibition of monopolistic trade practice;
- (iv) prohibition of restrictive trade practices.

The MRTP Act, 1969 underwent amendments in 1974, 1980, 1982, 1984, 1986, 1988 and 1991. Major changes introduced in the 1982 and 1984 Amendment Acts were based on the recommendations of the Sachar Committee. The 1984 amendment introduced the concept of unfair trade practice under the Act. Far-reaching changes have been brought about by the 1991 amendment and these were made in the wake of new industrial policy of July, 1991 which is wedded to liberalisation, globalisation and de-regulation.

#### *Scheme of the MRTP Act*

Prevention of undesirable concentration of economic power was sought to be achieved essentially through the regulation of growth of undertakings of particular size, viz. undertakings having assets of the value of Rs. 100 crores. These business houses were officially designated as large business houses. Undertakings having a sizable share of the market, or licensed production capacity of more than 1/4th of the total production or installed capacity in India were described as dominant undertakings. These companies were declared large business houses if their assets were of the value of Rs. 1 crore or more.

These undertakings were referred to as MRTP undertakings. Such undertakings had to obtain approval of the Central Government to undertake substantial expansion of production, establishment of new undertakings, amalgamate with or takeover any other undertaking. Appointment of persons who were

directors in such undertakings as director in any other undertaking needed the approval of the Central Government. The Central Government also had the power to order for division of such undertakings or for severance of interconnection under certain circumstances. Restrictions were placed on the acquisition and transfer of shares of, or by, bodies corporate owning such undertakings.

However, the MRTP (Amendment) Act, 1991 sought to liberalise these restrictions by removing the concept of MRTP undertakings and provisions relating to their substantial expansion, amalgamation etc., and acquisition of shares of, or by, such undertakings etc. The provisions relating to Central Government's power to direct division of undertakings or severance of interconnection have been modified such that they apply to all undertakings (hitherto, they applied only to MRTP undertakings).

Chapter IV deals with monopolistic trade practices indulged in by any undertaking. The Act defines the concept of monopolistic trade practices in terms of unreasonableness of the prices charged, unreasonableness in preventing or lessening competition in the market, unreasonably increasing prices, profits and limiting technical development to the common detriment etc. The remedy for dealing with monopolistic trade practice is an inquiry at the instance of the Central Government by the M.R.T.P. Commission or suo motu by the Commission and suitable orders being passed by the Central Government thereafter to prevent the mischief resulting from such practices.

The Act also deals with matters relating to restrictive trade practices. Briefly stated, a restrictive trade practice is one which prevents, distorts or restricts competition for goods and services in any manner. While unreasonableness is the test for monopolistic trade practices, even a small distortion in competition is sufficient to bring a case under restrictive trade practices. The provisions relating to restrictive trade practices are therefore intended to promote fair and free competition in the market. The Act provides for a scheme of registration of certain agreements relating to restrictive trade practices. The MRTP (Amendment) Act, 1984 introduced new provisions relating to unfair trade practices with a view to promoting the interest of consumers. It is essential to note that the M.R.T.P. Commission has been given full powers to regulate restrictive and unfair trade practices by means of an inquiry and pass final orders thereon. The MRTP Commission may inquire into restrictive and unfair trade practices at the instance of the Central Government, State Government, Director General of Investigation and Registration, registered consumer associations, individual consumer and on its own. The Commission has also powers to grant temporary injunctions and award compensation and punish for contempt under Sections 12A, 12B and 13B of the Act respectively.

The Commission is an independent quasi-judicial body and has powers similar to a Civil Court under the Code of Civil Procedure, 1908 on some matters. The Director General of Investigation and Registration and the Secretary of the Commission assist in the inquiry in respect of monopolistic, restrictive and unfair trade practices. The Commission conducts enquiries and other businesses in accordance with MRTPC Regulations, 1991.

The Central Government has framed the Monopolies and Restrictive Trade Practices Rules, 1970, the Monopolies and Restrictive Trade Practices (Classification of Goods) Rules, 1971, and the M.R.T.P. (Information) Rules, 1971 in exercise of the powers conferred under the Act. However these Rules have lost much of their significance in view of deletion of Sections 21 to 26 of the Act w.e.f. 27.9.91.

### **MRTP (Amendment) Act, 1991**

The new industrial policy announced by the Government in Parliament on July 24, 1991 sought to amend the MRTP Act, 1969 by removing all pre-entry restrictions and placing more emphasis on controlling and regulating monopolistic, restrictive and unfair trade practices.

The 'Statement of Objects and Reasons to the MRTP (Amendment) Act, 1991 reiterates that the basic

philosophy behind the MRTP Act, 1969 was not to inhibit industrial growth but to ensure that industrial growth was channelised for public good and growth did not perpetuate concentration of economic power to the common detriment. To quote,

1. With the growing complexity of industrial structure and the need for achieving economies of scale for ensuring higher productivity and competitive advantage in the international market, the thrust of the industrial policy has shifted to controlling and regulating the monopolistic, restrictive and unfair trade practices rather than making it necessary for certain undertakings to obtain prior approval of the Central Government for expansion, establishment of new undertakings, merger, amalgamation, take over and appointment of directors. It has been the experience of the Government that pre-entry restrictions under the MRTP Act on the investment decision of the corporate sector has outlived its utility and has become a hindrance to the speedy implementation of industrial projects. By eliminating the requirement of time-consuming procedures and prior approval of the Government, it would be possible for all productive sections of the society to participate in efforts for maximisation of production. It is, therefore, proposed to re-structure the MRTP Act by omitting the provisions of Sections 20 to 26 and transfer the provisions contained in Chapter III-A regarding restrictions on acquisition and transfer of shares to the Companies Act, 1956. The Schedule to the MRTP Act is also consequently to be transferred with modification to the Companies Act, 1956.
2. It is also proposed to enlarge the scope of inquiry by the MRTP Commission with a view to taking effective steps to curb and regulate monopolistic, restrictive and unfair trade practices which are prejudicial to public interest. It is also proposed to provide for deterrent punishment for contravention of the orders passed by the MRTP Commission and the Central Government and empower the Commission to punish for its contempt. Certain other consequential changes are also found necessary in the MRTP Act.

### Scope and Applicability of the MRTP Act

Section 3 of the MRTP Act, 1969 provides that unless the Central Government, by notification in the Official Gazette otherwise directs, the Act shall not apply to:

- (a) undertakings owned or controlled by the Government, a government company, a corporation, a registered cooperative society and undertakings the management of which has been taken over by the Central Government;
- (b) trade unions and other associations of workmen;
- (c) financial institutions.

However, vide notification dated 27.9.1991, the Government has directed that the provisions of the MRTP Act shall apply to all undertakings and financial institutions specified in Section 3 which were hitherto outside the purview of the Act, except undertakings owned or controlled by a Government company, or the Government and engaged in the production of arms and ammunition and allied items of defence equipment, defence aircraft and warships, atomic energy, minerals specified in the schedule to the Atomic Energy (Control of Production and Use) Order, 1953 and industrial units under the Currency and Coinage Division, Ministry of Finance, Department of Economic Affairs. Thus, the hitherto anomaly which used to exist prior to 27.9.91 about applicability of provisions of Act between private sector enterprises and public sector undertakings and those stated in sub-clause (a) to (g) of Section 3, has been removed.

But trade unions and other associations of workmen or employees formed for their own reasonable protection as such workmen or employees continue to be exempt from the applicability of the MRTP Act. However, Truck owners or operators Unions/Associations being not of workmen have been held to be

subject to the jurisdiction of MRTP Commission by Supreme Court in the case of Bharatpur Truck Operators Union.

In effect, all public sector companies, except those engaged in the production of arms and ammunition etc. and industries under the Currency and Coinage Division, have been brought within the scope of the MRTP Act in respect of monopolistic, restrictive and unfair trade practices.

## MONOPOLISTIC TRADE PRACTICES

Prohibition of monopolistic trade practices is one of the objects of the MRTP Act, 1969. The word 'monopoly' has not been defined in the MRTP Act. But it is common knowledge that a pure monopoly as well as 'monopolistic' position leads to distortion of competition in the market, besides endangering in the normal circumstances concerted action to fix prices, supplies of commodities, etc. The result of such action is no doubt detrimental to the consuming public.

*The Monopolies Inquiry Commission made copious analysis of this aspect in its report. It is worth quoting the following passages from Chapter V of the report:*

Our study of product-wise concentration brings out prominently the fact that in a large number of industries, a single undertaking is the only supplier or at least has to its credit a very large portion of the market as compared with its competitors. Such an undertaking has the power to dictate the price of the commodity or services it supplies and to regulate its volume of production in such a manner as to maximize its profits. This power is what is generally understood by the words "monopoly power" Though in the strict etymological sense of the word, and in strict economic theory, monopoly exists when there is only one single supplier, there is no reason why an enterprise enjoying the power to dictate the price and thus to control the market even though it is not the single supplier should not be considered a monopoly. What happens in such cases is that the price decided upon by the dominant producer (or distributor) is followed by others who are in a position to compete. This price leadership phenomenon is in essence a manifestation of the price leaders power to dictate the price in the market. We think it proper therefore to include within the word monopoly not only the single supplier in a market but also the one dominant supplier who has the power to dictate the price in the market."

"The question that next arises is : When such a power is shared by a few enterprises being the dominant sellers, should they be considered to be holding a monopolistic position? We see no reason to exclude such dominant sellers from our understanding of monopoly. For, the essence of monopoly is the ability to dictate the price and control the market without being materially influenced by other competing concerns."

One important difference between the situation when a single seller dominates the market and a few independent sellers together enjoy a dominating position cannot be overlooked. In the former case, monopoly power is inevitably present, in the latter it may or not be present. The effect on the market of a few dominant sellers has been widely discussed by economists, specially in recent years; but their opinions are by no means the same. We do not propose to try to resolve this controversy. It is sufficient for our purpose to notice that it is generally agreed that when a few big sellers dominate the market there will ordinarily be a high probability of their coming to some kind of agreement or understanding whether formal or not, about the price and output, by which a monopolistic power is shared between themselves. Even in the absence of such agreement or understanding it frequently happens that each has a healthy fear of the other big producers or distributors and ultimately a policy of live and let live comes into operation. Some economists point out that when a few large sellers dominate the market, each of them is able to calculate fairly and accurately the probable effect on the market of his action in increasing or decreasing his output. So, it is said that each will try to regulate the output in such a way that the marginal costs remain well below the price. Each such seller

will also be well aware that any attempt of his to reduce the price is likely to be met immediately by similar action by his competitors. The matter is succinctly put by Stocking in *Monopoly and Free Enterprise* at p. 90 thus:

"In markets where sellers are few, each in trying to determine his most profitable volume of output must, as would a monopolist, consider the probable effects of various possible rates of production not only on costs but also on prices. Indeed each seller will ordinarily decide on the price at which he will sell and adjust his output accordingly, just as a monopolist does. Each oligopolist however in determining his price must consider not merely his own cost-price relationships but also how his rivals will react to his prices. Anyone of a few sellers, if fully informed and perfectly rational, when selling a completely standardised product will realise that if he reduces his prices his rivals will meet the lower price promptly."

For all these reasons we are convinced that when the market is dominated by a few sellers, monopolistic conditions will sometimes prevail. At the same time, we are conscious that even in a market of a few sellers there will sometimes be keen competition. This is likely to happen apart from the effect of the mutual jealousies which sometimes characterise the relations between big business houses when one or more of the few sellers feel confident that due to superior managerial ability and technical skill and financial resources they will be able to capture a larger share of the market at the expense of their rivals. Even so there is no gainsaying the fact that in a market of a few dominating sellers there is real risk of the emergence of monopolistic power and consequently of monopolistic practices. To ascertain the extent to which monopolistic practices prevail, we must examine not only the cases where a single enterprise is the sole or dominant producer of the goods or services but also the cases where a few enterprises between themselves share such dominating position."

## RESTRICTIVE TRADE PRACTICES

The Monopolies and Restrictive Trade Practices Act, 1969, has as one of its objects the prohibition of restrictive trade practices. In order to ensure that the benefits of free and fair competition in a market reach the ultimate consumer, it is essential that the process of competition should not be distorted by any trade practice, either by a single manufacturer or a group of manufacturers or dealers. For instance, if a manufacturer stipulates a condition that the wholesale purchaser shall sell only his products and not of others or shall resell the goods only at the prices stipulated by him or forces the wholesale purchaser to procure the entire line of manufacture from him, the result may be a distortion of competition in the market. The MRTP Act is concerned with promoting fair and free competition in the market, the securing of consumer interest being the ultimate goal.

The Monopolies Inquiry Commission in its report observed that a restrictive trade practice means a practice which obstructs the free play of competitive forces or impedes the free flow of capital or resources into the stream of production or of the finished goods in the stream of distribution at any point before they reach the hands of the ultimate consumer. The Commission list out the following types of restrictive trade practices pursued not only in India but also in many other countries. These include (i) horizontal fixation of price (ii) vertical fixation of price and re-sale price maintenance; (iii) allocation of markets between purchasers; (iv) discrimination between purchasers; (v) boycott; (vi) exclusive dealing contracts; and (vii) tie-up arrangements.

The Monopolies Inquiry Commission made a wee-bit of distinction between a monopolistic trade practice and a restrictive trade practice. It observed every monopolistic trade practice is on the face of it a restrictive trade practice. Indeed, sometimes the two words are used indiscriminately. Thus the report of Macquarie Committee which was set up to study Canadian Combines Legislation treats all combines or common policy among several firms designed to strengthen the market position of a group of firms as monopolistic

practices. In our opinion, every practice whether it is by action or understanding or agreement, formal or informal, to which persons enjoying monopoly power resort in exercise of the same to reap the benefits of that power and every action, understanding or agreement tended to or calculated to preserve, increase or consolidate such power should properly be designated monopolistic trade practice.

## UNFAIR TRADE PRACTICES

Unfair trade practices in trade and commerce were prevalent even in older days. Priests in Sumaria and Babylon are on record to have lent money to the needy at high rates of interest. During the period of Tudors, practices of forestalling (meaning pushing up prices by buying up supplies before they reached market), regrating (buying up supplies in the market), and engrossing (buying up supplies wherever available) were prevalent. Thus exploitation at market place is not a new phenomena of modern civilisation. At present various types of unfair trade practices are prevalent at National as well as at International markets. The legislative history of countries the world over bears redeeming testimony to the endeavours of the National Governments to enact suitable legislations to curb such unfair trade practices.

The underlying objective of such legislative endeavours has been to make the behaviour at market place conducive to righteous dealings so that the ultimate consumer gets a fair deal. Senator Murphy, the then Australian Attorney General, introducing the Restrictive Trade Practices Bill of the Commonwealth of Australia in the Senate said: In consumer transactions, unfair practices are widespread. The existing law is still founded on the principle known as 'Caveat Emptor meaning 'let the buyer beware. That principle may have been appropriate for transactions conducted in village markets, it has ceased to be appropriate as a general rule. Now the marketing of goods and services is conducted on organised basis and by the trained business executives. The untrained consumer is no match for the businessman who attempts to persuade the consumer to buy goods or services on terms and conditions suitable to the vendor. The consumer needs protection by the law and this Bill will provide such protection.

It is often said that consumers need no special protection; all can be safely left to the market. But the concept of perfect market is an economists dream and consumers sovereignty a myth. In real life products are complex and of great variety and consumers and retailers have imperfect knowledge. Suppliers may often have a dominant buying position. As a consequence bargaining power in the market is generally weighed against the consumer. Thus consumers have felt the need to create organisations to identify their interests and to supply information and advice.

The Federal Trade Commission of US is stated to have labelled under the Federal Trade Commission Act, 1914 numerous practices not known before. It was because a need was felt to ensure that the public was prevented from being made victims of false claims of products blatantly advertised even though it may not have an adverse effect on the competition. The effort was to shift the emphasis on detection and eradication of fraud against the consumers, particularly those belonging to the weaker sections of the society.

## Consumer Protection Law in India

The Government enacted various laws to safeguard the interest of the consumers. The Essential Commodities Act, The Trade Marks Act, The Specific Relief Act, The Drugs Control Act, The Drugs and Cosmetics Act, The Drugs and Magic Remedies (Objectionable Advertisements) Act, The Emblems and Names (Prevention of Improper Use) Act, The Indian Standard Institution (Certification Marks) Act, The Agricultural Produce (Grading and Marketing) Act, The Standards of Weights and Measures Act, etc. are a few of the many laws intended to protect the interest of the consumer. Some of these laws alongwith the delegated legislation framed thereunder protect both the pecuniary interest as well as other interests of the consumer. Even the Indian Contract Act 1872 and the Sale of Goods Act, 1930 contain provisions for breach

of contracts and remedies therefor. The Indian Penal Code provides for stringent punishment for certain offences.

In the year 1986, the Government enacted the Consumer Protection Act, 1986 and framed necessary rules thereunder, for facilitating the formation of Consumer Protection Councils in all states and setting up of Consumer Forums at district level, State Commission at state level and National Commission at national level for redressing the grievances of consumers. The Government also framed the MRTP (Recognition of Consumer Association) Rules and amended a number of economic legislations like the Essential Commodities Act, 1955; Standards of Weights and Measures Act, 1976; Prevention of Food Adulteration Act, 1954; Drugs and Cosmetics Act, 1940 etc. to provide better protection to consumers.

However, the passing of the MRTP Act, 1969, could be said to be the beginning of the Government's concern for consumer interest. Till the amendment of the Act in the year 1984, even the MRTP Act did not contain provisions directly aimed at protecting the interests of consumer, but they were intended to regulate competition in the hope that it would generate fair conduct, the effect of which would percolate to the ultimate consumer, the terminal point in the distributive line.

### ***Recommendations of Sachar Committee***

The Government of India appointed a Committee in August, 1977 under the Chairmanship of Justice Rajinder Sachar to look into the simplification of the working of the companies and the MRTP Act. The Committee submitted its report in the year 1978 and as far as recommendations pertaining to the MRTP Act are concerned, far reaching changes were suggested by the Committee. For the first time, the Committee highlighted the need for introduction of suitable provisions to curb unfair trade practices.

In its view, the assumption that curbing monopolistic and restrictive trade practices and thereby preventing distortion of competition automatically results in the consumers getting a fair deal was only partly true. It was felt necessary to protect the consumers from practices adopted by trade and industry to mislead or dupe them.

The Committee pointed out that advertisements and sales promotion having become well established modes of modern business techniques, representations through such advertisements to the consumer should not become deceptive. If a consumer was falsely induced to enter into buying goods which do not possess the quality and did not have the cure for the ailment advertised, it was apparent that the consumer was being made to pay for quality of things on false representation. Such a situation could not be accepted.

Therefore, an obligation is to be cast on the seller to speak the truth when he advertises and also to avoid half truths, the purpose being preventing false or misleading advertisements.

The Committee also noted that fictitious bargain was another common form of deception and many devices were used to lure buyers into believing that they were getting something for nothing or at a nominal value for their money. The Committee observed: Prices may be advertised as greatly reduced and cut when in reality the goods may be sold at sellers regular prices. Advertised statements that could have two meanings, one of which is false, are also considered misleading. In America, it was held that statement that a tooth paste 'fights decay could be interpreted as a promise of complete protection and was thus deceptive. Mock-ups on television put up by companies including Colgate Palmolive had also received the attention of the Enforcement Agencies in America and have been held to be deceptive.

We cannot say that the type of misleading and deceptive practices which are to be found in other countries are not being practised in our country. Unfortunately our Act is totally silent on this aspect. The result is that the consumer has no protection against false or deceptive advertisements. Any misrepresentation about the quality of a commodity or the potency of a drug or medicine can be projected without much risk. This has

created a situation of a very safe heaven for the suppliers and a position of frustration and uncertainty for the consumers. It should be the function of any consumers legislation to meet this challenge specifically. Consumer protection must have a positive and active role.

Accordingly, the Committee specified certain unfair trade practices which were notorious and suggested prohibition of such practices. The main category of unfair trade practices recommended for prohibition by the Sachar Committee were: (a) misleading advertisements and false representations (b) bargain sale, bait and switch selling; (c) offering gifts or prizes with the intention of not providing them and conducting promotional contests; (d) supplying goods not conforming to safety standards; and (e) hoarding and destruction of goods.

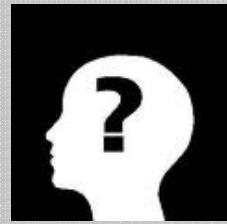
In India, by an amendment to the MRTP Act in the year 1984 Part B Unfair Trade Practices was added to Chapter V. It may be recalled that Part 'A' of Chapter V deals with registration of agreements relating to restrictive trade practices. Section 36A, 36B, 36C, 36D and 36E are relevant for the purposes of understanding the main provisions relating to unfair trade practices.

#### ***Scheme of the Act with respect to Unfair Trade Practices***

The term 'Unfair Trade Practices' is defined in Section 36A which enlists a number of practices as unfair trade practices. This definition has been amended vide the MRTP (Amendment) Act, 1991 making its scope wider in application. Section 36B provides for an enquiry into unfair trade practices by the MRTP Commission. Section 36C contains provision for preliminary investigation by the Director General in certain cases. Section 36D deals with the powers of the Commission to inquire into unfair trade practice and pass remedial orders. Section 36E empowers the Commission to exercise same powers in respect of unfair trade practices as it exercises in respect of restrictive trade practices.

#### ***Why do we need competition in the market?***

*Competition is now universally acknowledged as the best means of ensuring that consumers have access to the broadest range of services at the most competitive prices. Producers will have maximum incentive to innovate, reduce their costs and meet consumer demand. Competition thus promotes allocative and productive efficiency. But all this requires healthy market conditions and governments across the globe are increasingly trying to remove market imperfections through appropriate regulations to promote competition.*



## **COMPETITION ACT, 2002**

#### ***Short title, extent and commencement***

Section 1 of the Act provides that it shall come into force on such date as the Central Government may notify in the Official Gazette. However, an enabling provision empowering the Government to appoint different dates for different provisions of the Act have been incorporated. The scope of the Act extends to whole of India except the State of Jammu and Kashmir.

#### ***Scheme of the Act***

The Scheme of the Act has been split into nine chapters indicated hereunder: Chapter I contains preliminary provisions viz. Short title, extent and Definition clauses; Chapter II provides for substantive laws i.e. Anti Competitive Agreements, Abuse of Dominance and Regulation of Combinations; Chapter III contains provisions relating to Establishment of Commission, Composition of Commission, Selection of Committee for Chairperson and other Members, Term of Office of Chairperson etc. Chapter IV elaborately provides the

Duties, Powers and Functions of the Commission; Chapter V provides for the Duties of Director General; Chapter VI stipulates Penalties for Contravention of Orders of Commission, Failure to Comply with Directions of Commission and Director-General, Making False Statement or Omission to Furnish Material Information etc; Chapter VII deals with Competition Advocacy; Chapter VIII contains provisions relating to Finance, Accounts and Audit, Chapter VIII A contains provisions relating to "Competition Appellate Tribunal" [inserted by the Competition (Amendment) Act, 2007] and Chapter IX contains Miscellaneous provisions.

## DEFINITIONS

The important concepts incorporated in the Competition Act, 2002 have been defined under Section 2 of the Act. These have been discussed herein below:

### ***Acquisition***

This term has been specifically defined. It means – directly or indirectly, acquiring or agreeing to acquire: (i) shares, voting rights or assets of any enterprise; (ii) control over management or control over assets of any enterprise. [(Section 2(a)]

The terms 'acquiring' or 'acquisition' are relevant for "Regulation of Combinations".

### ***Agreement***

The term includes any arrangement or understanding or action in concert—

- (i) whether or not, such arrangement, understanding or concert is in formal or in writing; or
- (ii) whether or not such arrangement, understanding or concert is intended to be enforceable by legal proceedings.

It implies that an arrangement need not necessarily be in writing. The term is relevant in the context of Section 3, which envisages that anti-competitive agreements shall be void and thereby prohibited by the law. [Section 2(b)]

The term "Competition" is not defined in the Act. However, in the corporate world, the term is generally understood as a process whereby the economic enterprises compete with each other to secure customers for their product. In the process, the enterprises compete to outsmart their competitors, sometimes to eliminate their rivals. Competition in the sense of economic rivalry is unstable and has a natural tendency to give way to a monopoly. Thus, competition kills competition.

### ***Cartel***

"Cartel" includes an association of producers, sellers or distributors, traders or service providers who, by agreement amongst themselves, limit control or attempt to control the production, distribution, sale or price of or, trade in goods or provision of services. [Section 2(c)]

The nature of a cartel is to raise price above competitive levels, resulting in injury to consumers and to the economy. For the consumers, cartelisation results in higher prices, poor quality and less or no choice for goods or/and services.

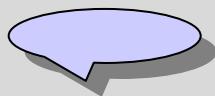
An international cartel is said to exist, when not all of the enterprises in a cartel are based in the same country or when the cartel affects markets of more than one country.

An import cartel comprises enterprises (including an association of enterprises) that get together for the purpose of imports into the country.

An export cartel is made up of enterprises based in one country with an agreement to cartelize markets in other countries. In the Competition Act, cartels meant exclusively for exports have been excluded from the provisions relating to anti-competitive agreements. This is because such cartels do not adversely affect markets in India and are hence outside the purview of the Competition Act.

If there is effective competition in the market, cartels would find it difficult to be formed and sustained.

***Some of the conditions that are conducive to cartelization are:***



- *high concentration - few competitors*
- *high entry and exit barriers*
- *homogeneity of the products (similar products)*
- *similar production costs*
- *excess capacity*
- *high dependence of the consumers on the product*
- *history of collusion*

***Chairperson***

Chairperson means the Chairperson of Competition Commission of India appointed under Sub-section (1) of Section 8. [Section 2(d)]

***Commission***

Commission means Competition Commission of India established under Section 7(1). [Section 2(e)]

***Consumer***

Under that Act, the Consumer includes only such purchasers or buyers who make purchases for their own consumption or to earn their livelihood. This deficiency has now been made good – by defining “Consumer” under the Act. Consumer means any person who—

- (i) 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 or promised or under any system of deferred payment when such use is made with the approval of such person, whether such purchase of goods is for resale or for any commercial purpose or for personal use.
- (ii) hires or avails of any services for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment when such services are availed of with the approval of the first mentioned person whether such hiring or availing of services is for any commercial purpose or for personal use. [Section 2(f)]

It may be noted that under the Competition Act even if a person purchases goods or avails of services for commercial purpose, he will be a Consumer, whereas for purposes of Consumer Protection Act, a person purchasing goods/availing services for commercial purposes is not a “Consumer” and can not seek relief under that Act.

**Director General**

Director General means the Director General appointed under Section 16(1) and includes Additional, Joint or Deputy or Assistant Director Generals. [Section 2(g)]

**Enterprise**

Enterprise means a person or a department of the Government, who or which is, engaged in any activity, relating to production, control of goods or articles or provision of services, of any kind, or in investment, or in the business of acquiring, holding, underwriting or dealing with shares, debentures or other securities whether such unit or division or subsidiary is located at the same place where the enterprise is located or at different place(s).

However, it does not include any activity of the Central Government relating to sovereign functions of Government including all activities carried on by the Government Departments dealing with atomic energy, currency, defence and space.

'Activity' includes profession or occupation. 'A unit or division' includes a plant or factory established for production, supply, distribution, acquisition or control of any goods or any branch or office established for provision of any service. [Section 2(h)]

It may thus be noted that sovereign function of Government are excluded from definition of enterprise but Government Departments performing non-sovereign functions for consideration are subject to jurisdiction of Commission.

**Goods**

Goods means goods as defined in Sale of Goods Act, 1930 and includes—

- (a) products manufactured, processed or mined;
- (b) debentures, shares and stocks after allotment;
- (c) in relation to 'goods supplied', goods imported into India. [Section 2(i)]

**Member**

Member means a Member of the Commission appointed under Section 8(1) of the Act and includes a Chairperson. [Section 2(j)]

**Notification**

Notification means notification published in the Official Gazette. [Section 2(k)]

**Person**

Person includes (i) an individual; (ii) a Hindu undivided family; (iii) a company; (iv) a firm; (v) an association of persons; (vi) a corporation established under Central, State Act or a Government Company (vii) a body corporate incorporated by or under a law of a foreign country; (viii) a co-operative society registered under any Law (ix) local authority (x) every artificial juridical person.

'Government Company' for this Section will be same as defined under Section 617 of Companies Act, 1956. [Section 2(p)]

### ***Practice***

Practice includes any practice relating to carrying on of any trade by a person or enterprise. [Section 2(p)]

### ***Prescribed***

Prescribed means prescribed by rules made under the Act by Central Government. [Section 2(n)]

### ***Price***

Price, in relation to sale of goods or supply of services, includes every valuable consideration, whether direct or indirect, or deferred, and includes any consideration, which relates to sale of any goods or to performance of any services although ostensibly relating to any other matter or thing. [Section 2(o)]

### ***Public Financial Institution***

Public Financial Institution means a Public Financial Institution as defined in Section 4A of Companies Act, 1956 and includes a State Financial, Industrial or Investment corporation. [Section 2(p)]

### ***Regulations***

Regulations means the regulations made by the Competition Commission of India. [Section 2(q)]

### ***Relevant Market***

Relevant market means the market, which may be determined by the Commission with reference to 'relevant product market' or 'relevant geographic market' or with reference to both the markets. [Section 2(r)]

### ***Relevant Geographic Market***

Relevant Geographic Market means a market comprising the area in which the conditions of competition for supply of goods or provision of services or demand of goods or services are distinctly homogenous and can be distinguished from conditions prevailing in neighbouring areas. [Section 2(s)]

### ***Relevant Product Market***

Relevant Product Market means a market comprising of all those products or services which are regarded as interchangeable or substitutable by the consumer, by reasons of characteristics of products or services, their prices and intended use. [Section 2(t)]

The terms 'relevant market', 'relevant geographical market' and 'relevant product market' have relevance in determination of the agreements being anti competitive, in evaluating combinations and dominance of an enterprise or group. An agreement in the nature of cartel which limits or controls production, supply, market, technical development, investments etc. need to be looked as being anti competitive with reference to relevant market. Similarly agreement to share the market or sources of production by way of allocation of geographical area of market, types of goods or services or number of customers in the market or by any similar way and these need to be interpreted in the context of the definition of relevant geographical market under Section 2(s).

### ***Service***

Service means service of any description which is made available to potential users and includes the

provision of services in connection with business of any industrial or commercial matters such as banking, communication, education, financing, insurance, chit funds, real estate, transport, storage, material treatment, processing, supply of electrical or other energy, boarding, lodging, entertainment, amusement, construction, repair, conveying of news or information and advertising. [Section 2(u)]

It may be noted that under the Competition Act, the services of industrial or commercial nature also fall within the scope of the Act whereas under the Consumer Protection Act, the services of commercial nature or for business or industrial purposes are excluded for interpreting deficiency in the supply thereof and for determining compensation, if any, payable to them. To this extent, the relief claimable under the Consumer Protection Act, 1986 is limited in scope. It may also be noted that "education" has been specifically included in ambit of "Service" to set at rest the dispute, if any, about the jurisdiction of Commission in such matters.

### **Shares**

Shares means shares in the share capital of a company carrying voting rights and includes, –

- (i) any security which entitles the holder to receive shares with voting rights;
- (ii) stock except where a distinction between stock and share is expressed or implied. [Section 2(v)]

This definition of shares is much wider than what is provided under the Companies Act. It implies that not only shares in the share capital of a company e.g. equity or preference shares are included in the definition of shares but 'debentures convertible into shares with voting rights' are also included.

### **Statutory Authority**

Statutory authority means any authority, board, corporation, council, institute, university or any other body corporate, established by or under any Central, State or Provincial Act for the purposes of regulating production or supply of goods or provision of any services or markets therefor or any matter connected therewith or incidental thereto. [Section 2(w)]

It implies that this definition widens the scope of type of bodies, which are empowered to make a reference for enquiring into anti-competitive agreement or abuse of dominant position or make a reference for opinion on a competition issue.

### **Trade**

Trade means any 'trade', business, industry, profession or occupation relating to production, supplies, distribution, storage or control of goods and includes the provision of any services.

The definition of the term 'trade' is relevant, inter-alia, to the interpretation of any of the type of agreement listed in Section 4 (a), (b), (c), (d) and (e) in relation to the trading goods and provisions of services. [Section 2(x)]

### **Turnover**

Turnover includes value of sale of goods or services. [Section 2(y)]

The definition of the term 'turnover', inter-alia, is relevant and significant in determining whether the combination of merging entities exceeds the threshold limit of the turnover specified in Section 5 of the Act. It is also relevant for the purpose of imposition of fines by the Commission.

Section 2 further provides that the words and expression used but not defined in the Competition Act, 2002

and defined in the Companies Act, 1956 [(1) of 1956] shall have the same meaning respectively assigned to them in the Companies Act, 1956 (1 of 1956).

Chapter II of the Competition Act, 2002 stipulates provisions relating to Prohibition of Certain Agreements, Abuse of Dominant Position and Regulations of Combinations.

### **Anti Competitive Agreements**

It is provided under Section 3(1) of the Competition Act that no enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition. Section 3(2) further declares that any anti competitive agreement within the meaning of sub-section 3(1) shall be void. Under the law, the whole agreement is construed as 'void' if it contains anti-competitive clauses having appreciable adverse effect on competition. Section 3(3) provides that following kinds of agreements entered into between enterprises or association of enterprises or persons or associations of persons or person or enterprise or practice carried on, or decision taken by any association of enterprises or association of persons, including "cartels", engaged in identical or similar goods or services which –

- (a) directly or indirectly determines purchase or sale prices;
- (b) limits or controls production, supply, markets, technical development, investment or provision of services;
- (c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or type of goods or services, or number of customers in the market or any other similar way; and
- (d) directly or indirectly results in bid rigging or collusive bidding;

shall be presumed to have an appreciable adverse effect on the competition and onus to prove otherwise lies on the defendant.

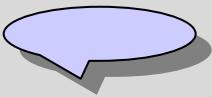
The explanation appended to the Section 3 defines the term 'bid rigging' as any agreement between enterprises or persons which has the effect of eliminating or reducing competition for bids or adversely affecting or manipulating the process for bidding. Efficiency enhancing joint ventures entered into by parties engaged in identical or similar goods or services, shall not be presumed to have appreciable adverse effect on competition but judged by rule of reason. The term "cartel" used in the Section is the most severe form of entering into 'anti competitive agreements' and has been defined in Section 2(c).

Bid rigging takes place when bidders collude and keep the bid amount at a pre-determined level. Such pre-determination is by way of intentional manipulation by the members of the bidding group. Bidders could be actual or potential ones, but they collude and act in concert.

### **Bid rigging is anti-competitive**

Bidding, as a practice, is intended to enable the procurement of goods or services on the most favourable terms and conditions. Invitation of bids is resorted to both by Government (and Government entities) and private bodies (companies, corporations, etc.). But the objective of securing the most favourable prices and conditions may be negated if the prospective bidders collude or act in concert. Such collusive bidding or bid rigging contravenes the very purpose of inviting tenders and is inherently anti-competitive.

**Some of the most commonly adopted ways in which collusive bidding or bid rigging may occur are:**



- *agreements to submit identical bids*
- *agreements as to who shall submit the lowest bid, agreements for the submission of cover bids (voluntarily inflated bids)*
- *agreements not to bid against each other,*
- *agreements on common norms to calculate prices or terms of bids*
- *agreements to squeeze out outside bidders*
- *agreements designating bid winners in advance on a rotational basis, or on a geographical or customer allocation basis*

If bid rigging takes place in Government tenders, it is likely to have severe adverse effects on its purchases and on public spending. Bid rigging or collusive bidding is treated with severity in the law. The presumptive approach reflects the severe treatment.

Section 3(4) provides that any agreement amongst enterprises or persons at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or price of, or trade in goods or provision of services, including —

- (a) tie-in agreement;
- (b) exclusive supply agreement;
- (c) exclusive distribution agreement;
- (d) refusal to deal;
- (e) resale price maintenance;

shall be an agreement in contravention of sub-section (1) if such agreement causes or is likely to cause an appreciable adverse effect on competition in India.

The term “**tie-in agreement**” includes any agreement requiring a purchaser of goods, as a condition of such purchase, to purchase some other goods. A good example of tie-in agreement is where a gas distributor requires a consumer to buy a gas stove as a pre condition to obtain connection of domestic cooking gas. [*Chanakaya and Siddharth Gas company, In-re RTP 11/1985* decided by (MRTCP Commission on 27.1.1985)]

“**Exclusive supply agreement**” includes any agreement restricting in any manner from acquiring or otherwise dealing in any goods other than those of the seller or any other person. Thus, where a manufacturer asks a dealer not to deal in similar products of its competitor directly or indirectly and discontinues the supply on the ground that dealer also deals in product of suppliers’ competitor’s goods is an illustration of exclusive dealing agreement. [*Bhartia Curtec Hammer Ltd. In-re (1997) 24 CLA 104 (MRTPC)*]

“**Exclusive distribution agreement**” includes any agreement to limit, restrict or withhold the output or supply of any goods or allocate any area or market for the disposal or sale of the goods.

Requiring a distributor not to sell the goods of the manufacturer beyond the prescribed territory is a good example of exclusive distribution agreement. *Vadilal Enterprise Ltd. In-re (1998 (91) COMP CAS 824* is a good example of exclusive distribution agreement.

**“Refusal to deal”** includes any agreement, which restricts, or is likely to restrict, by any method the persons or classes of persons to whom goods are sold or from whom goods are bought. For eg. an agreement which provides that the franchisees will not deal in products or goods of similar nature for a period of three years from the date of determination of agreement within a radius of five kms from showroom amounts to exclusive dealing agreement. *DGIR v. Titan industries (2001) 43 CLA 293 MRTPC*.

**“Resale price maintenance”** includes any agreement to sell goods on condition that the prices to be charged on resale by the purchaser shall be the prices stipulated by the seller unless it is clearly stated that prices lower than those prices may be charged.

Any stipulation that the cement dealer should not sell below the stipulated price is a ‘resale price maintenance’ practice and is an anti competitive practice. (*In re-India Cement Ltd. RTP Inquiry 48 /1985*).

The agreements falling in Section 3(3) shall be presumed to have appreciable adverse affect on competition and thereby they are construed as deemed restrictive agreements. The agreements falling in Section 3(4) shall be judged by rule of reason and the onus lies on the prosecutor to prove its appreciable adverse effect on competition. The definition of all restrictive concepts covered under Section 3(4) is inclusive one.

Moreover, Section 3 does not restrict the right of any person to restrain any infringement of or to impose reasonable conditions, as may be necessary for protecting any of his rights which have been or may be conferred upon him under—

- (a) the Copyright Act, 1957;
- (b) the Patents Act, 1970;
- (c) the Trade and Merchandise Marks Act, 1958 or the Trade Marks Act, 1999;
- (d) the Geographical Indications of Goods (Registration and Protection) Act, 1999;
- (e) the Designs Act, 2000;
- (f) the Semi-conductor Integrated Circuits Layout-Design Act, 2000.

That apart, the Act does not restrict any person’s right to export from India goods under an agreement which requires him to exclusively supply, distribute or control goods or provision of services for fulfilling export contracts. The exclusion of ‘export business’ is in view of ‘effect theory’, and doctrine of ‘relevant market’.

### **WHAT IS AN ANTI-COMPETITIVE AGREEMENT?**

*An anti-competitive agreement is an agreement having appreciable adverse effect on competition. Anti-competitive agreements include, but are not limited to:-*

- *agreement to limit production and/or supply;*
- *agreement to allocate markets;*
- *agreement to fix price;*
- *bid rigging or collusive bidding;*
- *conditional purchase/ sale (tie-in arrangement);*
- *exclusive supply / distribution arrangement;*
- *resale price maintenance; and*
- *refusal to deal.*



### Prohibition of abuse of dominant position

Section 4 of the Competition Act, 2002 expressly prohibits any enterprise or group from abusing its dominant position, meaning thereby a position of strength, enjoyed by an enterprise or group, in the relevant market, in India, which enables it to—

- (i) operate independently of competitive forces prevailing in the relevant market; or
- (ii) affect its competitors or consumers or the relevant market in its favour”.

In line with the latest global trend, the dominance shall not be determined with reference to “assets”, “turnover” or “market share”.

As per Section 2(r) ‘relevant market’ means the market, which may be determined by the Commission with reference to the relevant ‘product market’ or ‘relevant geographic market’ or with reference to both the markets. Thus, for determining dominance, these are relevant concepts.

The term “enterprise” means a person or a department of the Government, who or which is, or has been, engaged in any activity, relating to the production, storage, supply, distribution, acquisition or control of articles or goods, or the provision of services, of any kind, or in investment, or in the business of acquiring, holding, underwriting or dealing with shares, debentures or other securities of any other body corporate, either directly or through one or more of its units or divisions or subsidiaries, whether such unit or division or subsidiary is located at the same place where the enterprise is located or at a different place or at different places, but does not include any activity of the Government relatable to the sovereign functions of the Government including all activities carried on by the departments of the Central Government dealing with atomic energy, currency, defence and space.

For the purposes of this clause, “activity” includes profession or occupation; “article” includes a new article and “service” includes a new service; “unit” or “division”, in relation to an enterprise, includes—

- (i) a plant or factory established for the production, storage, supply, distribution, acquisition or control of any article or goods;
- (ii) any branch or office established for the provision of any service.

Section 4(2) states that there shall be abuse of dominant position, if an enterprise or group —

- (a) directly or indirectly imposes unfair or discriminatory;
  - (i) condition in purchase or sale of goods or services; or
  - (ii) price in purchase or sale (including predatory price) of goods or service.

Explanation appended to Section 4 (2) clarifies that the unfair or discriminatory condition in purchase or sale of goods or services shall not include any discriminatory condition or price which may be adopted to meet the competition.

Section 4(2)(b) includes in abuse of dominant position an enterprise or group limiting or restricting

- (i) production of goods or provision of services or market therefore; or
- (ii) technical or scientific development relating to goods or services to the prejudice of consumers.

Similarly Section 4 (2) (c), (d) and (e) specify three other forms of abuses namely, if any person indulges in practice or practices resulting in denial of market access in any manner; or makes conclusion of contracts subject to acceptance by other parties of supplementary obligations which, by their nature or according to

commercial usage, have no connection with the subject of such contracts and also, if any person uses dominant position in one relevant market to enter into, or protect, other relevant market.

The term “predatory price” has been defined as the sale of goods or provision of services, at a price which is below the cost, as may be determined by regulations, of production of goods or provision of services, with a view to reduce competition or eliminate the competitors. Thus, the two conditions precedent to bring a case with the ambit of predatory pricing are:

- (i) selling goods or provision of service at a price which is below its cost of production and
- (ii) that practice is resorted to eliminate the competitors or to reduce competition.

The Competition Commission of India has been empowered under Section 19(4) of the Act to determine whether any enterprise or group enjoys a dominant position or not, in the ‘relevant market’ and also to decide whether or not there has been an abuse of dominant position. It may be noted that mere existence of dominance is not to be frowned upon unless the dominance is abused.

### **WHAT CONSTITUTES ABUSE OF DOMINANCE?**

*Dominance refers to a position of strength which enables an enterprise to operate independently of competitive forces or to affect its competitors or consumers or the market in its favour. Abuse of dominant position impedes fair competition between firms, exploits consumers and makes it difficult for the other players to compete with the dominant undertaking on merit. Abuse of dominant position includes:*



- *imposing unfair conditions or price,*
- *predatory pricing,*
- *limiting production/market or technical development ,*
- *creating barriers to entry,*
- *applying dissimilar conditions to similar transactions,*
- *denying market access, and*
- *using dominant position in one market to gain advantages in another market.*

### **Combinations**

Combination has broad coverage and includes acquisition of control, shares, voting rights, assets, merger or amalgamation. The acquisition of one or more enterprises by one or more person or merger or amalgamation of enterprises shall be a combination of such enterprises and persons or enterprises, if –

- (a) any acquisition where—
  - (i) the parties to the acquisition, being the acquirer and the enterprise, whose control, shares, voting rights or assets have been acquired or are being acquired jointly have, -
    - (A) either, in India, the assets of the value of more than rupees one thousand crores or turnover more than rupees three thousand crores; or
    - (B) in India or outside India, in aggregate, the assets of the value of more than five hundred million US dollars, including at least rupees five hundred crores in India or turnover more than fifteen hundred million US dollars, including at least rupees fifteen hundred crores in India; or

- (ii) the group, to which the enterprise whose control, shares, assets or voting rights have been acquired or are being acquired, would belong after the acquisition, jointly have or would jointly have, -
  - (A) either in India, the assets of the value of more than rupees four thousand crores or turnover more than rupees twelve thousand crores; or
  - (B) in India or outside India, in aggregate, the assets of the value of more than two billion US dollars, including at least rupees five hundred crores in India or turnover more than six billion US dollars, including at least rupees fifteen hundred crores in India; or
- (b) acquiring of control by a person over an enterprise when such person has already direct or indirect control over another enterprise engaged in production, distribution or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service, if -
  - (i) the enterprise over which control has been acquired along with the enterprise over which the acquirer already has direct or indirect control jointly have,
    - (A) either in India, the assets of the value of more than rupees one thousand crores or turnover more than rupees three thousand crores; or
    - (B) in India or outside India, in aggregate, the assets of the value of more than five hundred million US dollars, including at least rupees five hundred crores in India or turnover more than fifteen hundred million US dollars, including at least rupees fifteen hundred crores in India; or
  - (ii) the group, to which enterprise whose control has been acquired, or is being acquired would belong after the acquisition, jointly have would jointly have,
    - (A) either in India, the assets of the value of more than rupees four thousand crores or turnover more than rupees twelve thousand crores; or
    - (B) in India or outside India, in aggregate, the assets of the value of more than two billion US dollars, including at least rupees five hundred crores in India or turnover more than six billion US dollars including at least rupees fifteen hundred crores in India; or
- (c) any merger or amalgamation in which—
  - (i) the enterprise remaining after merger or the enterprise created as a result of the amalgamation, as the case may be, have,
    - (A) either in India, the assets of the value of more than rupees one thousand crores or turnover more than rupees, three thousand crores; or
    - (B) in India or outside India, in aggregate, the assets of the value of more than five hundred million US dollars, including at least rupees five hundred crores in India or turnover more than fifteen hundred million US dollars, including at least rupees fifteen hundred crores in India; or
  - (ii) the group, to which the enterprise remaining after the merger or the enterprise created as a result of the amalgamation, would belong after the merger or the amalgamation, as the case may be, have or would have,
    - (A) either in India, the assets of the value or more than rupees four thousand crores or turnover more than rupees twelve thousand crores; or
    - (B) in India or outside India, the assets of the value of more than two billion US dollars

including at least rupees five hundred crores in India or turnover more than six billion US dollars, including at least rupees fifteen hundred crores in India.

It may be pointed out that "control" for the purposes of this section includes controlling the affairs or management by — (i) one or more enterprises, either jointly or singly, over another enterprise or group; (ii) one or more groups, either jointly or singly, over another group or enterprise.

The term "group" means two or more enterprises, which, directly or indirectly, are in a position to—

- (i) exercise less than fifty percent of voting rights in other enterprise; or
- (ii) appoint more than fifty per cent of the members of the board of directors in other enterprise; or
- (iii) control the management or affairs of the other enterprise.

It is further provided that the "value of the assets" shall be determined on the basis of the value of assets as shown in the audited books of account of the enterprise, in the financial year immediately preceding the financial year in which the date of proposed merger falls, after deducting any depreciation therefrom. The value of the assets shall also include the brand value, value of goodwill, or value of copyright, patent, permitted use, collective mark, registered proprietor, registered trade mark, registered user, geographical indications, design or layout design or similar other commercial rights, referred to in Section 3(5).

It is clear from the above that two kinds of norms have been prescribed which would attract Section 5. Firstly, the "value of asset" and secondly the "turnover" in India or outside India. In the case of a "group" the "assets" or "turn over" of the "group" has to be aggregated and in the case of "merger" or "amalgamation" the value of the "assets" or "turn over" of the resultant entity has to be computed in case the parties do not belong to a 'group'. In case a party belongs to a group, the assets or turnover of the group and the merged or amalgamated entity could belong. It is also noteworthy that the control may be either by one or more enterprises over another enterprise or a group or one or more groups singly or jointly over another group or enterprise. It is also significant to note that while computing the value of the assets both 'physical assets' and the intangible ones such as 'goodwill' or 'trade mark' etc. will be taken into account in determining whether reporting requirements get triggered or not.

In exercise of the powers conferred by the sub section (3) of Section 20 of the Competition Act, 2002, the Central Government in consultation with the Competition Commission of India, vide its Notification S.O. 480(E) dated 4<sup>th</sup> March, 2011 enhance, on the basis of Wholesale Price Index, the value of assets and the value of turnover, by fifty per cent for the purposes of Section 5 of the Act.

The Central Government, in Public interest, exempts an enterprise, whose control, shares, voting rights or assets are being acquired has assets of the value of not more than Rs. 250 crores or turnover of not more than Rs. 750 crores from the provisions of Section 5.

### **WHAT IS COMBINATION?**

*Broadly, combination under the Act means acquisition of control, shares, voting rights or assets, acquisition of control by a person over an enterprise where such person has direct or indirect control over another enterprise engaged in competing businesses, and mergers and amalgamations between or amongst enterprises when the combining parties exceed the thresholds set in the Act. The thresholds are specified in the Act in terms of assets or turnover in India and outside India. Entering into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India is prohibited and such combination shall be void.*



**Threshold of Combination specifies under section 5 of the Act in tabular form given below as per notification S.O.480 (E), dated 4.3.2011:**

In India	APPLICABLE TO	ASSETS		TURNOVER	
		₹ 1,500 cr.	₹ 4,500 cr.	₹ 6,000 cr.	₹ 18,000 cr.
	ASSETS		TURNOVER		
In India and outside		Total	Minimum Indian Component	Total	Minimum Indian Component out of Total
		\$ 750 m	₹ 750 cr.	\$ 2,250 m	₹ 2,250 cr.
		Group	₹ 750 cr.	9 bn.	₹ 2,250 cr.

(Source: [www.cci.gov.in](http://www.cci.gov.in))

### Regulation of Combinations

Section 6 of the Competition Act prohibits any person or enterprise from entering into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and if such a combination is formed, it shall be void. Section 6(2) envisages that any person or enterprise, who or which proposes to enter into any combination, shall give a notice to the Commission disclosing details of the proposed combination, in the form, prescribed and submit the form together with the fee prescribed by regulations. Such intimation should be submitted within 30 days of—

- (a) approval of the proposal relating to merger or amalgamation, referred to in Section 5(c), by the board of directors of the enterprise concerned with such merger or amalgamation, as the case may be;
- (b) execution of any agreement or other document for acquisition referred to in Section 5(a) or acquiring of control referred to in Section 5(b).

A newly inserted sub-section (2A) envisages that no combination shall come into effect until 210 days have passed from the day of notice or the Commission has passed orders, whichever is earlier.

The Competition Commission of India (CCI) has been empowered to deal with such notice in accordance with provisions of Sections 29, 30 and 31 of the Act. Section 29 prescribes procedure for investigation of combinations. Section 30 empowers the Commission to determine whether the disclosure made to it under Section 6(2) is correct and whether the combination has, or is likely to have, an appreciable adverse effect on the competition. Section 31 provides that the Commission may allow the combination if it will not have any appreciable adverse effect on competition or pass an order that the combination shall not take effect, if in its opinion, such a combination has or is likely to have an appreciable adverse effect on competition.

The provisions of Section 6 do not apply to share subscription or financing facility or any acquisition, by a public financial institution, foreign institutional investor, bank or venture capital fund, pursuant to any covenant of a loan agreement or investment agreement. This exemption appears to have been provided in

the Act to facilitate raising of funds by an enterprise in the course of its normal business. Under Section 6(5), the public financial institution, foreign institutional investor, bank or venture capital fund, are required to file in prescribed form, details of the control, the circumstances for exercise of such control and the consequences of default arising out of loan agreement or investment agreement, within seven days from the date of such acquisition or entering into such agreement, as the case may be.

As per the explanation appended to Section 6(5)

- (a) "foreign institutional investor" has the same meaning as assigned to it in clause (a) of the Explanation to Section 115AD of the Income-tax Act, 1961;
- (b) "venture capital fund" has the same meaning as assigned to it in clause (b) of the Explanation to clause (23 FB) of Section 10 of the Income-tax Act, 1961.

It may be noted that under the law, the combinations are only regulated whereas anti-competitive agreements and abuse of dominance are prohibited. Further, under the MRTP Act prior to 27.9.91, undertakings of certain size were required to be registered and such undertakings were required to seek prior approval of the Central Government before embarking upon expansion plans. In the present Act, there is no requirement of registration of an undertaking and further, there is no need to have prior approval of the Central Government but CCI will only examine as to whether or not combination is or is likely to have an appreciable adverse effect on competition.

The Competition Act with many innovative concepts coupled with power to impose fine is likely to let in harsh glare of sunlight to disinfect pernicious anti-competitive practices.

### **Competition Commission of India**

#### *Establishment of Commission*

The Central Government under Section 7 has been empowered to establish a Commission to be called "Competition Commission of India" by issue of a Notification. The Commission is a body corporate having perpetual succession and a common seal. The Commission has power to acquire, hold movable or immovable property and to enter into contract in its name and by the said name, sue or be sued. In the premises, the set up of Commission corresponds to that of Securities & Exchange Board of India constituted under the SEBI Act, 1992.

The Head Office of the Commission shall be at such place as the Central Government may decide from time to time. Vide Notification: SO 1198(E) dated 14<sup>th</sup> Oct., 2003, the Central Government established the Competition Commission of India having its Head Office at New Delhi.

The Commission has also been authorized to establish its office at other places in India. Thus, the law provides for setting up of CCI's offices at places other than that of its Headquarter.

#### *Composition of Commission*

The composition of the Commission as spelled out under Section 8 of the Act consists of a Chairperson and not less than two and not more than six other Members. The Chairperson and the Members are to be appointed by the Central Government. Regarding the qualifications of the Chairman and other Members, Section 8(2) provides that they shall be person of ability, integrity and standing and who has special knowledge of and such professional experience of not less than fifteen years in international trade, economics, business, commerce, law, finance, accountancy, management, industry, public affairs or competition matters including competition law and policy which in the opinion of the Central Government, may be useful to the commission. The Chairperson and other Members are to be appointed on whole time basis.

### *Selection of Chairperson and Members of Commission*

Section 9(1) envisages that the Chairperson and other Members of the Commission shall be appointed by the Central Government from a panel of names recommended by a Selection Committee consisting of the Chief Justice of India or his nominee, as Chairperson; and the Secretary in the Ministry of Corporate Affairs, Member; the Secretary in the Ministry of Law and Justice, Member; and two experts of repute who have special knowledge of, and professional experience in international trade, economics, business, commerce, law, finance, accountancy, management, industry, public affairs or competition matters including competition law and policy, as member.

### *Term of office of Chairperson and other Members*

The Act stipulates that the Chairperson and every other Member shall hold office as such for a term of five years from the date on which he enters upon his office and shall be eligible for re-appointment. However, the Chairperson or other Members shall not hold office as such after he has attained the age of sixty-five years.

A vacancy caused by the resignation or removal of the Chairperson or any other Member under section 11 or by death or otherwise shall be filled by fresh appointment in accordance with the provisions of sections 8 and 9. The Chairperson and every other Member shall, before entering upon his office, make and subscribe to an oath of office and of secrecy in such form, manner and before such authority, as may be prescribed.

In the event of the occurrence of a vacancy in the office of the Chairperson by reason of his death, resignation or otherwise, the senior-most Member shall act as the Chairperson, until the date on which a new Chairperson, appointed in accordance with the provisions of this Act to fill such vacancy, enters upon his office. When the Chairperson is unable to discharge his functions owing to absence, illness or any other cause, the senior-most Member shall discharge the functions of the Chairperson until the date on which the Chairperson resumes the charge of his functions.

### *Resignation of Chairperson etc.*

It has been provided under section 11 that the Chairperson or any other Member may resign his office by notice in writing under his hand addressed to the Central Government. However, until the Chairperson or a Member is permitted by the Central Government to relinquish his office, he will continue to hold his office until the expiry of three months from the date of receipt of such notice or until a person duly appointed as a successor enters into his office or until the expiry of his term, which ever is the earliest. Under Section 11(2), it is provided that in the following circumstances the Central Government may, by order, remove the Chairperson or any Member from his office if such Chairman or Member as the case may be, -

- (a) is, or at any time has been, adjudged as an insolvent; or
- (b) has engaged at any time, during his term of office, in any paid employment; or
- (c) has been convicted of an offence which, in the opinion of the Central Government, involves moral turpitude; or
- (d) has acquired such financial or other interest as it likely to affect prejudicially his functions as a Member; or
- (e) has so abused his position as to render his continuance in office prejudicial to the public interest; or
- (f) has become physically or mentally incapable of acting as a Member.

However, no Member shall be removed from his office on the ground that he has acquired such financial or other interest as is likely to affect prejudicially his function as a Member or has so abused his position as to

render his continuance in public office prejudicial to the public interest unless the Supreme Court, on a reference being made to it in this behalf by the Central Government, has on an inquiry as prescribed reported that the Member ought on such ground or grounds to be removed.

Section 12 provides that for a period of two years from the date on which the Chairperson and other Member cease to hold office shall not accept any appointment in or connected with the management or administration of, any enterprise which has been a party to the proceeding before the Commission. This restriction, however, shall not apply to any employment under the Central Government or a State Government or local authority or any corporation established by or under any Central, State or Provincial Act or a Government company as defined in Section 617 of the Companies Act, 1956 (10 of 1956).

#### *Financial and Administrative Powers of Member Administration*

A Member of the Commission as per Section 13 may be designated by the Central Government as Member Administration who shall exercise such financial and administrative powers as may be vested in him under the rules made by the Central Government. However, the Member Administration shall have authority to delegate such of his financial and administrative powers to any other officer of the Commission as he may deem fit subject to the condition that, while exercising delegated powers such official shall continue to act under the direction, superintendence and control of the Member Administration.

#### *Salary and Terms and Conditions of Service*

The salary allowances and other terms and conditions of service of the Chairman and other member including travel expenses, house rent allowance, conveyance facility, sumptuary allowance and medical facilities shall be such as may be prescribed. Further, to ensure freedom in the functioning of the Chairperson and the Member, Section 14(2) provides that the salary allowance and other terms and conditions of service of the Chairperson or Member shall not be varied to his disadvantage after his appointment.

No act or proceedings of the Commission shall be invalid merely because there is any vacancy in the Commission or defect in the constitution of the Commission; or any defect in the appointment of Chairperson or a Member; or any irregularity in the procedure of the Commission not affecting the merits of the case.

#### *Appointment of Director General*

Director General is an important functionary under the Act. He is to assist the Commission in conducting inquiry into contravention of any of the provisions of the Act and for performing such other functions as are, or may be, provided by or under the Act.

Section 16 (1) empowers the Central Government to appoint a Director General and such number of additional, joint, deputy or assistant Director Generals or other advisers, consultants or officers for the purposes of assisting the Commission in conducting inquiry into the contravention of any provision of the Act.

Additional, joint, deputy and assistant Director Generals, other advisors, consultants and officers shall however, exercise powers and discharge functions subject to the general control, supervision and directions of the Director General.

The salary, allowances and other terms and conditions and service of Director General, consultants, advisers or other officers assisting him shall be such as may be prescribed by the Central Government. The Director General, advisers, consultants and officers assisting him are to be appointed from amongst the persons of integrity and outstanding ability and who have experience in investigation, and knowledge of accountancy, management, business, public administration, international trade, law or economics and such other qualifications as may be prescribed.

The Commission may appoint a Secretary and such officers and other employees, as it considers necessary for the efficient performance of his functions under the Act. The Commission may engage, in accordance with the procedure specified by regulations, such number of experts and professionals of integrity and outstanding ability, who have special knowledge of, and experience in, economics, law, business or such other disciplines related to competition, as it deems necessary to assist the Commission in the discharge of its functions under the Act.

#### ***Duties, Powers and Functions of Commission***

As per Section 18 of the Act, duties of the CCI are:—

- (a) to eliminate practices having adverse effect on competition;
- (b) to promote and sustain competition;
- (c) to protect interests of consumers and
- (d) to ensure freedom of trade carried on by other participants, in markets in India.

Section 18 empowers the Commission to enter into any memorandum or arrangement, with the prior approval of the Central Government, for the purpose of discharging the duties and functions under this Act with any agency of any foreign country. This will enable the CCI to have extra territorial reach and shall facilitate exchange of information and enforcement of its order.

#### ***Inquiry into certain agreements and dominant position of enterprise***

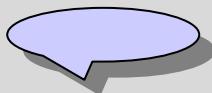
The Commission may inquire into any alleged contravention of Section 3(1) or 4(1) on its own motion or on

- (a) receipt of any information in such manner and accompanied by such fee, from any person, consumer or consumer association or trade association; or
- (b) a reference made to it by the Central Government or State Government or a statutory authority.

The Director General is not vested with a right to move an application for institution of an enquiry relating to anti-competitive agreements or abuse of dominance.

The terms 'person' and 'statutory authority' have been defined under Sections 2(l) and 2(w) respectively. The term 'person' has been given wide connotation and it includes an individual, a HUF, a company, a firm, an association of persons, any corporation established under any Central, State or Provincial Act or a Government company, a co-operative society, a local authority and every artificial juridical person.

***Section 19(3) provides that while determining whether an agreement has appreciable adverse effect on competition, the Commission shall give due regard to all or any of the following factors, namely—***

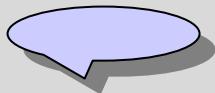


- (a) creation of barriers to new entrants in the market;
- (b) driving existing competitors out of the market;
- (c) foreclosure of competition by hindering entry into the market;
- (d) accrual of benefits to consumers;
- (e) improvements in production or distribution of goods or provision of services;
- (f) promotion of technical, scientific and economic development by means of production or distribution of goods or provision of services.

The first three factors are anti-competitive, while the latter three factors deal with benign effects.

“Adverse appreciable affect on competition” is a key factor while enquiring into anti-competitive agreement. The touch stone of appreciable adverse effect on competition need not be proved while enquiring into abuse of dominance.

***For the purpose of determining whether an enterprise enjoys dominant position or not under Section 4, the Commission shall have due regard to all or any of the following factors, namely –***



- (a) market share of the enterprise;
- (b) size and resources of the enterprise;
- (c) size and importance of the competitors;
- (d) economic power of the enterprise including commercial advantages over competitors;
- (e) vertical integration of the enterprises or sale or service network of such enterprises;
- (f) dependence of consumers on the enterprise;
- (g) monopoly or dominant position whether acquired as a result of any statute or by virtue of being a Government company or a public sector undertaking or otherwise;
- (h) entry barriers including barriers such as regulatory barriers, financial risk, high capital cost of entry, marketing entry barriers, technical entry barriers, economies of scale, high cost of substitutable goods or service for consumers;
- (i) countervailing buying power;
- (j) market structure and size of market;
- (k) social obligations and social costs;
- (l) relative advantage, by way of the contribution to the economic development, by the enterprise enjoying a dominant position having or likely to have an appreciable adverse effect on competition;
- (m) any other factor which the Commission may consider relevant for the inquiry.

The present law makes explicit the issues and the parameters which will be considered while deciding “abuse of dominance”. The Commission shall have due regard to the, “relevant geographic market” and “relevant product market” for determining as to what constitutes a “relevant market”.

The terms ‘relevant market’ and “relevant geographic market” have been defined in Sections 2 (r) and 2(s) of the Act. ***For determining the “relevant geographic market”, the Commission shall have due regard to all or any of the following factors, namely;—***

- (a) regulatory trade barriers;

- (b) local specification requirements;
- (c) national procurement policies;
- (d) adequate distribution facilities;
- (e) transport costs;
- (f) language;
- (g) consumer preferences;
- (h) need for secure, regular supplies or rapid after-sales service.

***Similarly, while determining ‘relevant product market’ the Commission shall have due regard to all or any of the following factors namely;***

- (a) physical characteristics or end-use of goods;
- (b) price of goods or service;
- (c) consumer preferences;
- (d) exclusion of in-house production;
- (e) existence of specialized producers;
- (f) classification of industrial products.

The prescription of parameters for determining “appreciable adverse effect” on competition of agreement, “dominant position”, within “relevant market”, are intended to bring consistency and certainty in the working of the Commission which has to consider all or any of the applicable factors, as the case may be. It is quite apparent that any inquiry by the CCI will be a detailed exercise, which will not only involve gathering of information in regard to technological or marketing factors but also the government policy which relate to the trade or business in which the enterprise is involved beside global scenario especially with regard to regulatory trade barriers including import-export policy, tariff and subsidy issues will also be taken into account by the Commission.

### **Inquiry into Combination by Commission**

The Commission under Section 20 of the Competition Act may inquire into the appreciable adverse effect caused or likely to be caused on competition in India as a result of combination either upon its own knowledge or information (suo motu) or upon receipt of notice under Section 6(2) relating to acquisition referred to in Section 5(a) or acquiring of control referred to in Section 5(b) or merger or amalgamation referred to in Section 5(c) of the Act. It has also been provided that an enquiry shall be initiated by the Commission within one year from the date on which such combination has taken effect. Thus, the law has provided a time limit within which suo moto inquiry into combinations can be initiated. This provision dispels the fear of enquiry into combination between merging entities after the expiry of stipulated period.

On receipt of the notice under Section 6(2) from the person or an enterprise which proposes to enter into a combination, it is mandatory for the Commission to inquire whether the combination referred to in that notice, has caused or is likely to cause an appreciable adverse effect on competition in India.

***The Commission shall have due regard to all or any of the factors for the purposes of determining whether the combination would have the effect of or is likely to have an appreciable adverse effect on competition in the relevant market, namely—***



- (a) *actual and potential level of competition through imports in the market;*
- (b) *extent of barriers to entry into the market;*
- (c) *level of combination in the market;*
- (d) *degree of countervailing power in the market;*
- (e) *likelihood that the combination would result in the parties to the combination being able to significantly and sustainably increase prices or profit margins;*
- (f) *extent of effective competition likely to sustain in a market;*
- (g) *extent to which substitutes are available or are likely to be available in the market;*
- (h) *market share, in the relevant market, of the persons or enterprise in a combination, individually and as a combination;*
- (i) *likelihood that the combination would result in the removal of a vigorous and effective competitor or competitors in the market;*
- (j) *nature and extent of vertical integration in the market;*
- (k) *possibility of a failing business;*
- (l) *nature and extent of innovation;*
- (m) *relative advantage, by way of the contribution to the economic development, by any combination having or likely to have appreciable adverse effect on competition;*
- (n) *whether the benefits of the combination outweigh the adverse impact of the combination, if any.*

The above yardsticks are to be taken into account irrespective of fact whether an inquiry is instituted, on receipt of notice under Section 6(2) upon its own knowledge. The scope of assessment of adverse effect on competition will be confined to the “relevant market”. Most of the facts enumerated in Section 20 (4) are external to an enterprise. It is noteworthy that sub clause (n) of Section 20 (4) requires to invoke principles of a “balancing”. It requires the Commission to evaluate whether the benefits of the combination outweigh the adverse impact of the combination, if any. In other words if the benefits of the combination outweigh the adverse effect of the combination, the Commission will approve the combination. Conversely, the Commission may declare such a combination as void.

#### **Reference by statutory authority**

The term “statutory authority” has been defined in Section 2(w). If in the course of a proceeding before any statutory authority, an issue is raised by any party that any decision which such authority has taken or proposes to take, is or would be, contrary to the provisions of the Competition Act 2002, it may make a reference in respect of such issue to the Commission and seek its opinion. The Commission shall, on receipt

of the reference, after hearing the parties to the proceedings, give its opinion within 60 days of receipt of such reference to such authority on the issues referred to it. The statutory authority shall thereafter pass such order on the issues referred to the Commission as it deems fit. The statutory authority may, *suo motu* make such reference in respect of such issue to the Commission. Likewise, the Commission either in the course of proceedings before it or *suo motu* may make a reference for opinion to a statutory authority and the latter has to render its opinion within 60 days of making a reference.

### **Meetings of Commission**

Section 22 provides that the Commission shall meet at such times and places, and shall observe such rules and procedure in regard to the transaction of business at its meetings as may be provided by regulations. The Chairperson, if for any reason, is unable to attend a meeting of the Commission, the senior-most Member present at the meeting, shall preside at the meeting. All questions which come up before any meeting of the Commission shall be decided by a majority of the Members present and voting, and in the event of an equality of votes, the Chairperson or in his absence, the Member presiding, shall have a second or/casting vote. However, the quorum for such meeting shall be three Members.

### **Procedure for inquiry on complaints under Section 19**

If the Commission is of the opinion that there exists a *prima facie* case, on receipt of an information from any person, consumer, their association or trade association or on a reference from Central Government or State Government or of a statutory authority or on its knowledge or information under Section 19, it shall direct the Director General to cause an investigation to be made into the matter. The Director General shall investigate into the matter and submit a report of its findings within the period as may be specified by the Commission. It is, however, not binding on the Commission to accept the report of the Director General.

Where upon receipt of a reference or information, the Commission is of the opinion that there is no *prima facie* case, it shall pass an order dismissing the reference/information, as it deems fit and necessary.

Upon receipt of a report from the Director General, the Commission shall forward a copy thereof to (a) the parties concerned or (b) Central Government or (c) State Government or (d) statutory authority as the case may be. If the Director General, in relation to a matter referred to it, recommends that there is no contravention of any of the provisions of the Act, the Commission shall give an opportunity of hearing to the informant and after hearing, if the Commission agrees with the recommendation of the Director General, it shall dismiss the information. According to Section 26(7) if, after hearing information provider, the Commission is of the opinion that further inquiry is called for, it shall direct the enquiry to proceed further.

Where the report of the Director General relates to matter referred to Commission by the Central Government or a State Government or a statutory authority and the report contains recommendation that there is no contravention of the provisions of the Act, the Commission shall invite the comments of the Central Government or the State Government or statutory authority, as the case may be, on such report. On receipt of the comments, if there is no *prima facie* case, in the opinion of the Commission the Commission shall return the reference. However, if the Commission feels that there is a *prima facie* case it shall proceed with a reference.

Section 26(9) provides that the Commission on receipt of recommendation of Director General that there is contravention of any of the provisions of the Act, and a further inquiry is called for, shall inquire into such contravention in accordance with the provisions of the Act.

The provisions of the Section indicate that it is mandatory that information or reference received or a matter which comes to the knowledge of the Commission regarding alleged violation of the provisions of the Act,

must be referred to the Director General for an investigation in the matter. A copy of the report of the Director General is required to be sent to the information provider or to the Central Government or State Government or a statutory authority, as the case may be, for their comments and an opportunity of hearing is required to be given to the parties as this is warranted by the principles of natural justice. Where the Director General recommends that there is contravention of any of the provisions of the Act, and that the Commission is of opinion that further inquiry is called for, it shall institute an inquiry into the matter and pass a reasoned order. The Commission may or may not subscribe to the recommendations of the Director General.

### ***Orders by Commission after inquiry into agreements or abuse of dominant position***

Section 27 envisages that the Commission after any inquiry into agreement entered into by any enterprise or association of enterprises or person or association of persons, or an inquiry into abuse of dominant position may pass all or any of the following orders, namely,—

- (i) direct that such agreement, or abuse of dominant position shall be discontinued and such agreement, which is in contravention of Section 3 shall not be re-entered or the abuse of dominant position in contravention of Section 4 shall be discontinued, as the case may be. The direction to discontinue and not to recur is commonly known as “Cease & desist” order.
- (ii) the Commission may impose penalty not exceeding ten percent of the average turnover of last three preceding financial years, upon each of person or enterprises which are parties to such agreement in contravention of Section 3 or are abusing dominant position within meaning of Section 4.

In case any agreement which is prohibited by Section 3 has been entered into by any cartel, the Commission may impose upon each producer, seller, distributor, trader or service provider participating in that cartel, a penalty up to three times of its profits for each year of the continuance of such agreement whichever is higher.

- (iii) The Commission may direct that the agreements shall stand modified to the extent and in the manner as specified in the order.
- (iv) The Commission may direct the enterprises concerned to comply with such other orders and directions, including payment of cost, if any, as it deems fit.
- (v) to pass such order or issue such directions as it may deem fit.

### ***Division of enterprise enjoying dominant position***

The Commission may, notwithstanding anything contained in any other law for the time being in force, by order in writing, direct division of an enterprise enjoying dominant position to ensure that such enterprise or group does not abuse its dominant position.

The order of the Commission referred to above may provide for all or any of the following matters, namely—

- (a) the transfer or vesting of property, rights, liabilities or obligations;
- (b) the adjustment of contracts either by discharge or reduction of any liability or obligation or otherwise;
- (c) the creation, allotment, surrender or cancellation of any shares, stocks or securities;
- (d) the formation or winding up of an enterprise or the amendment of the memorandum of association or articles of association or any other instruments regulating the business of any enterprise;
- (e) the extent to which, and the circumstances in which, provisions of the order affecting an enterprise may be altered by the enterprise and the registration thereof;
- (f) any other matter which may be necessary to give effect to the division of the enterprise or group.

### Procedure for investigation of combination

The procedure for investigation by the Commission has been stipulated under Section 29 of the Act. It involves following stages -

- (i) The Commission first has to form a *prima facie* opinion that a combination is likely to cause, or has caused an appreciable adverse effect on competition within the relevant market in India. Further, when the Commission has come to such a conclusion then it shall proceed to issue a notice to the parties to the combination, calling upon them to show cause why an investigation in respect of such combination should not be conducted;
- (ii) After receipt of the response of the parties to the combination may call for the report of the Director General.
- (iii) When pursuant to response of parties or on receipt of report of the Director General whichever is later, the Commission *prima-facie* is of the opinion that the Combination is likely to cause an appreciable adverse effect on competition in relevant market, it shall, within seven days direct the parties to the combination to publish within ten working days, the details of the combination, in such manner as it thinks appropriate so as, to bring to the information of public and persons likely to be affected by such combination.
- (iv) The Commission may invite any person affected or likely to be affected by the said combination, to file his written objections within fifteen working days of the publishing of the public notice, with the Commission for its consideration.
- (v) The Commission may, within fifteen working days of the filing of written objections, call for such additional or other information as it deem fit from the parties to the said combination and the information shall be furnished by the parties above referred within fifteen days from the expiry of the period notified by the Commission.
- (vi) After receipt of all the information and within forty-five days from expiry of period for filing further information, the Commission shall proceed to deal with the case, in accordance with provisions contained in Section 31 of the Act.

Thus, the provisions of Section 29 provide for a specified timetable within which the parties to the combination or parties likely to be affected by the combination are required to submit the information or further information to the Commission to ensure prompt and timely conduct of the investigation. It further imposes on Commission a time limit of forty-five working days from the receipt of additional or other information called for by it under sub-Section (4) of Section 29 for dealing with the case of investigation into a combination, which may have an adverse effect of the competition.

### ***Inquiry into disclosures under Section 6(2)***

Section 6(2) casts an allegation on any person or enterprise, who or which proposes to enter into combination, shall give notice to the Commission, in the form as may be specified, and the fee which may be determined, by regulations, disclosing the details of the proposed combination within thirty days of—

- (i) approval of the proposal relating to merger or amalgamation by the board of directors of the enterprises concerned with such merger or amalgamation;
- (ii) execution of any agreement or other document for acquisition referred to in Section 5(a) or acquiring of control referred to in Section 5(b).

Non-filing of notice attracts penalty in terms of Section 43A of the Act.

The newly inserted section 6(2A) envisages that no combination shall come into effect until two hundred and ten days have passed from the day on which notice has been given to Commission or the Commission has passed orders, whichever is earlier.

Upon receipt of such notice, the Commission shall examine such notice and form its *prima facie* opinion as to whether the combination has, or is likely to have, an appreciable adverse effect on the competition in the relevant market in India.

### ***Orders of Commission on Certain Combinations***

The Commission, after consideration of the relevant facts and circumstances of the case under investigation, by it under Sections 28 or 30 and assessing the effect of any combination on the relevant market in India, may pass any of the written orders indicated herein below. Where the Commission comes to a conclusion that any combination does not, or is not likely to, have an appreciable adverse effect on the Competition in relevant market in India, it may, approve that Combination.

- (i) In the case where the Commission is of the opinion that the combination has, or is likely to have an adverse effect on competition, it shall direct that the combination shall not take effect.
- (ii) Where the Commission is of the opinion that adverse effect which has been caused or is likely to be caused on competition can be eliminated by modifying such Combination then it shall direct the parties to such combination to carry out necessary modifications to the Combination.
- (iii) The parties accepting the proposed modification shall carry out such modification within the period specified by the Commission.
- (iv) Where the parties who have accepted the modification, fail to carry out such modification within the period specified by the Commission, such combination shall be deemed to have an appreciable adverse effect on competition and shall be dealt with by the Commission in accordance with the provisions of the Act.
- (v) If the parties to the Combination do not accept the proposed modification such parties may within thirty days of modification proposed by the Commission, submit amendment to the modification proposed by the Commission.
- (vi) If the Commission agrees with the agreement submitted by the parties it shall, by an order approve the combination.
- (vii) If the Commission does not accept the amendment then, parties shall be allowed a further period of thirty days for accepting the amendment proposed by the Commission.
- (viii) Where the parties to the combination fail to accept the modification within thirty days, then it shall be deemed that the combination has an appreciable adverse effect on Competition and will be dealt with in accordance with the provisions of the Act.
- (ix) Where the Commission directs under Section 31 (2) that the combination shall not take effect or it has, or is likely to have an appreciable adverse effect, it may order that,
  - (a) the acquisition referred to in Section 5 (a); or
  - (b) the acquiring of control referred to in Section 5(b); or
  - (c) the merger or the amalgamation referred to in Section 5(c) shall not be given effect to by the parties.

As per proviso the Commission may, if it considers appropriate, frame a scheme to implement its order in regard to the above matters under Section 31(10).

- (x) A deeming provision has been introduced by Section 31(11). It provides that, if the Commission does not, on expiry of a period of two hundred ten days from the date of filing of notice under Section 6(2) pass an order or issue any direction in accordance with the provisions of Section 29(1) or Section 29(2) or Section 29(7), the combination shall be deemed to have been approved by the Commission. In reckoning the period of two hundred ten days, the period of thirty days specified in Section 29(6) and further period of thirty working days specified in Section 29(8) granted by Commission shall be excluded.
- (xi) Further more where extension of time is granted on the request of parties the period of two hundred ten days shall be reckoned after the deducting the extended time granted at the request of the parties.
- (xii) Where the Commission has ordered that a combination is void, as it has an appreciable adverse effect on competition, the acquisition or acquiring of control or merger or amalgamation referred to in Section 5, shall be dealt with by other concerned authorities under any other law for the time being in force as if such acquisition or acquiring of control or merger or amalgamation had not taken place and the parties to the combination shall be dealt with accordingly.
- (xiii) Section 29(14) makes it clear that nothing contained in Chapter IV of the Act shall affect any proceeding initiated or may be initiated under any other law for the time being in force. It implies that provisions of this Act are in addition to and not in derogation of provisions of other Acts.

Thus, approval under one law does not make out a case for approval under another law.

### **Acts taking place outside India but having an effect on Competition in India**

Section 32 extends the jurisdiction of Competition Commission of India to inquire and pass orders in accordance with the provisions of the Act into an agreement or dominant position or combination, which is likely to have, an appreciable adverse effect on competition in relevant market in India, notwithstanding that,

- (a) an agreement referred to in Section 3 has been entered into outside India; or
- (b) any party to such agreement is outside India; or
- (c) any enterprise abusing the dominant position is outside India; or
- (d) a combination has taken place outside India; or
- (e) any party to combination is outside India; or
- (f) any other matter or practice or action arising out of such agreement or dominant position or combination is outside India.

The above clearly demonstrates that acts taking place outside India but having an effect on competition in India will be subject to the jurisdiction of Commission. The Competition Commission of India will have jurisdiction even if both the parties to an agreement are outside India but only if the agreement, dominant position or combination entered into by them has an appreciable adverse effect on competition in the relevant market of India.

### **Appearance before Commission**

As per Section 35 of the Act, following persons are entitled to appear before the Commission—

- (i) a complainant; or
- (ii) a defendant; or
- (iii) the Director General

They may either appear in person or authorise any of the following:

- (a) a chartered accountant as defined in Section 2(1)(b) of Chartered Accountants Act, 1949 (38 of 1949) who has obtained a certificate of practice; or
- (b) a company secretary as defined in Section 2(1)(c) of the Company Secretaries Act, 1980 (56 of 1980) and who has obtained a certificate of practice;
- (c) a cost accountant as defined in Section 2(1)(b) of the Cost and Works Accountants Act, 1959 (23 of 1959) and who has obtained a certificate of practice;
- (d) a legal practitioner that is an advocate, vakil or an attorney of any High Court including a pleader in practice.

*The above provisions unambiguously state that a 'Company Secretary in Practice' is entitled to represent an informant or a defendant or Director General. A Company Secretary in Practice can also get himself empanelled with the Director General to prosecute his cases before the Commission.*

### **Power of Commission to regulate its own procedure**

The Competition Commission of India has been empowered to lay down its own procedure and regulations. It is not bound by the procedure laid down by the Code of Civil Procedure, 1908 but shall have to observe the principles of natural justice and subject to the provisions of the Act. The Competition Commission of India shall also be subject to the rules made by the Central Government. Section 36(2) makes it clear that the Commission shall have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 while trying the suit, in respect of the following matters, namely:

- (a) summoning and enforcing the attendance of any person and examining him on oath;
- (b) requiring the discovery and production of documents;
- (c) receiving evidence on affidavits;
- (d) issuing commissions for the examination of witnesses or documents;
- (e) subject to the provisions of Sections 123 and 124 of the Indian Evidence Act, 1872, requisitioning any public record or document or copy of such record or document from any office;

In terms of Section 36(3), the Commission may call upon such experts, from the field of economics, commerce, accountancy, international trade or from any discipline as it deems necessary to assist the Commission in the conduct of any enquiry by it.

In terms of Section 36(4), the Commission may direct any person –

- (a) to produce before the Director General or the Secretary or an officer authorized by it, such books, or other documents in the custody or under the control of such person so directed as may be specified or described in the direction, being documents relating to any trade, the examination of which may be required for the purposes of the Act;
- (b) to furnish to the Director General or the Secretary or any other officer authorized by it, as respects the trade or such other information as may be in his possession in relation to the trade carried on by such person, as may be required for the purposes of the Act.

The Competition Commission is thus empowered to appoint experts, from the fields of economics, commerce, accountancy, international trade or from any other discipline as it deems necessary, to assist in the conduct of any inquiry or proceeding before it.

As stated earlier, Director General is an important functionary assisting the Commission and the Commission may ask the Director General to investigate into any trade practice and for the purpose of examination of books, or account and other document of the parties concerned. The Director General is also vested with all the powers as are conferred upon the Commission under Section 36(2) of Act.

### **Ratification of orders**

The Commission may amend any order passed by it under the provisions of this Act with a view to rectifying any mistake apparent from the record. Section 38(2) provides that subject to other provisions of this Act, the Commission may make –

- (a) an amendment of an order of its own motion;
- (b) an amendment for rectifying any mistake apparent from record, which has been brought to its notice by any party to the order.

An explanation below the Section clarifies that while rectifying any mistake apparent from the record, the Commission shall not amend substantive part of the order passed by it under the provisions of this Act.

### **Execution of Orders of the Commission Imposing Monetary penalty**

Section 39 provides that if a person fails to pay any monetary penalty imposed on him under the Act, the Commission shall proceed to recover such penalty, in such manner as may be specified by the regulations. In a case where the Commission is of the opinion that it would be expedient to recover the penalty imposed under the Act in accordance with the provisions of the Income-tax Act, 1961, it may make a reference to this effect to the concerned income-tax authority under that Act for recovery of the penalty as tax due under the said Act.

Where a reference has been made by the Commission under sub-section (2) for recovery of penalty, the person upon whom the penalty has been imposed shall be deemed to be the assessee in default under the Income Tax Act, 1961 and the provisions contained in sections 221 to 227, 228A, 229, 231 and 232 of the said Act and the Second Schedule to that Act and any rules made there under shall, in so far as may be, apply as if the said provisions were the provisions of this Act and referred to sums by way of penalty imposed under this Act instead of to income-tax and sums imposed by way of penalty, fine, and interest under the Income-tax Act, 1961 and to the Commission instead of the Assessing Officer.

*Explanation 1* – Any reference to sub-section (2) or sub-section (6) of section 220 of the income-tax Act, 1961 (43 of 1961), in the said provisions of that Act or the rules made thereunder shall be construed as references to sections 43 to 45 of this Act.

*Explanation 2* – The Tax Recovery Commissioner and the Tax Recovery Officer referred to in the Income-tax Act, 1961 shall be deemed to be the Tax Recovery Commissioner and the Tax Recovery Officer for the purposes of recovery of sums imposed by way of penalty under this Act and reference made by the Commission under sub-section (2) would amount to drawing of a certificate by the Tax Recovery Officer as far as demand relating to penalty under this Act.

*Explanation 3* – Any reference to appeal in Chapter XVIID and the Second Schedule to the Income-tax Act, 1961 shall be construed as a reference to appeal before the Competition Appellate Tribunal under section 53B of this Act.

It would be noted that Commission may by its Regulations has been empowered to evolve procedure of recovering monetary penalty. It may also make reference to Income Tax Authority for recovering of penalty as tax due under the said Act.

As per Section 39 every order passed by the Commission under this Act shall be executed in the same manner as if it were a decree or order made by the High Court or the Principal Civil Court in any suit pending therein.

It shall be lawful for the Commission to send, in event of its inability to execute it such order to the High Court or to the Principal Civil Court, as the case may be, within the limits of whose jurisdiction—

- (a) in the case of an order passed against any company or firm; the registered office or the sole or principal office of the business of company in India or where a company also has a subordinate office, that subordinate office, is situated;
- (b) in the case of an order passed against any other person, the place, where he voluntarily resides or carries on business or personally works for gain, is situated.

There upon the court to which the order is so sent shall execute the order as if it were a decree or order sent to it for execution.

### **Duties of Director General**

The Act provides that the Director General when so directed by the Commission, is to assist the Commission in investigation into any contravention of the provisions of this Act. The Director General is bound to comply with such a direction to render requisite assistance to the Commission.

The Director General, in order to effectively discharge his functions, has been given the same powers as are conferred upon the Commission under section 36(2). Under section 36(2) the Commission is having same powers as are vested in Civil Court under the Code of Civil Procedure (1908) while trying a suit, in respect of the following matters, namely;

- (a) summoning and enforcing the attendance of any person and examining him on oath;
- (b) requiring the discovery and production of documents;
- (c) receiving evidence on affidavits;
- (d) issuing commissions for the examination of witnesses or documents;
- (e) subject to the provisions of Sections 123 and 124 of the Indian Evidence Act, 1872, requisitioning any public record or document or copy of such record or document from any office;

Without prejudice to the above powers, the provisions of Sections 240 and 240A of the Companies Act, 1956, so far as may be, shall apply to an investigation made by the Director General or by a person authorised by him, as they apply to an inspector under the Companies Act 1956. This power includes search and seizure of the record of any person in respect of which an investigation has been directed by the Commission. It has been provided that wherever the approval of the Central Government is required, the same shall be given by the Commission and the word 'magistrate' appearing in Section 240A shall be construed as the Chief Metropolitan Magistrate.

### **Penalties**

The Competition Act prescribes penalties for contravention of orders of the Commission. As per Section 42, the Commission may cause an inquiry to be made into compliance of its orders or directions and—

- (a) if any person, without any reasonable cause, fails to comply with any order of the Commission, or

condition or restriction subject to which any approval, sanction, direction or exemption in relation to any matter has been accorded, given, made or granted under this Act; or

- (b) if any person fails to pay the penalty imposed under the Act,

he shall be punishable with imprisonment for a term which may extend to three years or with fine which may extend to rupees twenty five crores or with both, as the Chief Metropolitan Magistrate may deem fit. The Chief Metropolitan Magistrate, Delhi, however, shall not take cognizance of any offence save as a complaint filed by Commission or any of its officers authorized by it.

### **Compensation in case of Contravention of Orders of commission**

Section 42A provides that without prejudice to the provisions of this Act, any person may make an application to the Appellate Tribunal for an order for the recovery of compensation from any enterprise for any loss or damage shown to have been suffered, by such person as a result of the said enterprise violating directions issued by the Commission or contravening, without any reasonable ground, any decision or order of the Commission issued under sections 27, 28, 31, 32 and 33 or any condition or restriction subject to which any approval, sanction, direction or exemption in relation to any matter has been accorded, given, made or granted under this Act or delaying in carrying out such orders or directions of the Commission.

### ***Penalty for failure to comply with directions of Commission and Director General***

Section 43 of the Act provides that if any person fails to comply, without reasonable cause, with a direction given by the Commission under Sub-sections (2) and (4) of section 36; or the Director General while exercising powers referred to in sub-section (2) of section 41, such person shall be punishable with fine which may extend to rupees one lakh for each day during which such failure continues subject to a maximum of rupees one crore, as may be determined by the Commission

### ***Power to impose penalty for non-furnishing of information on combination***

Section 43A provides that if any person or enterprise who fails to give notice to the Commission under sub-section(2) of section 6, the Commission shall impose on such person or enterprise a penalty which may extend to one per cent of the total turnover or the assets, whichever is higher, of such a combination.

Thus, failure to file notice of combination falling under Section 5 attract deterrent penalty.

### ***Penalty for making false statement***

Section 44 provides that If any person, being a party to a combination, makes a statement which is false in any material particular, or knowing it to be false; or omits to state any material particular knowing it to be material, such person shall be liable to a penalty which shall not be less than rupees fifty lakhs but which may extend to rupees one crore, as may be determined by the Commission.

### ***Power to impose lesser penalty***

If any producer, seller, distributor, trader or service provider included in any cartel, which is alleged to have violated Section 3, has made a full and true disclosure in respect of alleged violations and such a disclosure is vital, the Commission may impose upon him a lesser penalty than as prescribed under the Act or rules or regulations.

However, the lesser penalty shall not be imposed where before making such disclosure, the report of Director General under Section 26 has been received in the Commission. Further, the lesser penalty shall be imposed only in respect of the producer, seller, distributor, trader or service provider included in the cartel, who has made a full, true and vital disclosures under this Section. Any producer, seller, trader or service

provider included in the cartel shall also be liable to imposition of penalty, if in the course of proceedings, had,—

- (a) not complied with the condition on which the lesser penalty was imposed by the Commission; or
- (b) given false evidence; or
- (c) the disclosure made is not vital.

The lesser penalty is for a member of a ring who breaks the rank. There is no provision to provide any protection or incentive to a whistle blower, which is conferred upon Authorities in contemporary legislations abroad.

The Act does not vest power in the Commission to compound an offence as was the position under the MRTP Act. It is viewed that long drawn investigation and enquiries could be arrested by provision such as compounding which allows an offence to be settled quickly. The Commission is also not vested with power to contempt.

### **Contravention by Companies**

A company means a body corporate and includes a firm or other association of individuals; director, in relation to a firm, means a partner in the firm for the purposes of penalties in connection with contravention of the provisions of the Act by companies.

Where any rule, regulation, order made by the Commission or any direction issued thereunder is contravened by a company, every person who, at the time the contravention was committed, was in charge, and was responsible to the company for conducting business of the company, as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished. However it will be a good defence by a person liable to any punishment if he proves that the contravention was committed without his knowledge or that he has exercised all due diligence to prevent the commission of an offence.

Where a contravention of any of the provisions of this Act or any rule, regulation, order made or direction issued thereunder has been committed by a company and it is proved that contravention has taken place with the consent or connivance of, or it is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly.

The word company in this Section, has been used in a wider sense and also includes a 'firm' or an 'association of persons'. Though the word 'director' is normally used in a company, in the light of the wider definition, the term director is interpreted to include a partner of the firm. The company being a legal person, its affairs are conducted by a board of directors, manager, secretary or other officer, therefore, according to Section 48 (2) such director, manager, secretary or other officer, in addition to the company itself shall be deemed to be liable to be proceeded against for contravention of any provisions of this Act or any rule, regulation, order made or direction issued thereunder by the Commission or the Director General of Investigation.

### **Competition Advocacy**

Under Section 49 the Central Government/State Government may seek the opinion of the CCI on the possible effects of the policy on competition or any other matter. In this context, Section 49 envisages that while formulating a policy on the competition, the Government may make a reference to the Commission for its opinion on possible effect of such a policy on the competition, or any other matter.

On receipt of such a reference, the Commission shall, give its opinion on it to the Central Government/State Government, within sixty days of making such a reference and the latter may formulate the policy as it deems fit. The role of the Commission is advisory and the opinion given by the Commission shall not be binding upon the Central Government/State Government in formulating such a policy. The Commission is also empowered to take suitable measures for the

- (a) promotion of competition advocacy;
- (b) creating awareness about the competition; and
- (c) imparting training about competition issues.

The creating awareness about benefits of competition and imparting training in competition issues is expected to generate conducive environment to promote and foster competition, which is sine-qua non for accelerating economic growth.

### **Finance, Accounts and Audit**

#### *Grants by Central Government*

The Central Government may make to the Commission grants of such sums of money as it may think fit for being utilised for the purposes of the Act. Such grant is to be made after due appropriation made by the Parliament.

#### *Constitution of Fund*

The Act provides for the constitution of a fund called the "Competition Fund" for meeting the establishment and other expenses of the Competition Commission in connection with the discharge of its functions and for the purposes of this Act. The following shall be credited to the "Competition Fund", -

- (a) all government grants received by the commission;
- (b) Omitted
- (c) the fees received under the Act;
- (d) the interest on the amounts accrued on the monies referred under clauses (a) to (c).

#### **Fee realized alongwith notice disclosing combination shall form part of 'Competition Fund'.**

The Fund shall be administered by a Committee of such Members of the Commission, as may be determined by the Chairperson and the Committee so appointed, shall spend monies out of the Fund only for the objects for which the Fund has been constituted.

#### *Accounts and Audit*

Proper accounts and other relevant records shall be maintained by the Commission and an annual statement of accounts shall be prepared by it in prescribed form in consultation with the Comptroller and Auditor General of India (CAG). The CAG shall specify the intervals within which the accounts of the Commission shall be audited by him.

Explanation to Section 52(2) clarifies that the orders passed by the Commission, being matters appealable to the Supreme Court, shall not be subject to audit by the CAG. The expenses, if any, incurred in connection with such audit shall be payable by the Commission to the CAG.

The CAG or any person appointed by him in connection with the audit of the accounts of the Commission shall have same rights, privileges and authority in connection with such audit as CAG has in connection with

the audit of Government accounts and, shall have the right to demand the production of books, accounts, connected vouchers and other documents and papers and to inspect any of the offices of the Commission.

Only accounts as certified by the CAG and any other person authorised by him in this behalf together with the audit report thereon shall be forwarded to the Central Government and the Government shall cause it to be laid before each House of Parliament.

#### *Furnishing of Returns, etc., to Central Government*

The Commission shall furnish to the Central Government such returns and statements and such particulars in regard to any proposed or existing measures for promotion of competition advocacy, creating awareness and imparting training about competition issues, in such form and such manner as the Central Government may prescribe. An annual report giving a true and full account of activities of the Commission during the previous year shall be prepared once in every year by the Commission and submitted to the Central Government.

A copy of the annual report of the Commission received by the Government shall cause to be laid by the Central Government before each House of Parliament.

### **COMPETITION APPELLATE TRIBUNAL**

Section 53A empowers the Central Government to establish, by notification, an Appellate Tribunal to be known as Competition Appellate Tribunal –

- (a) to hear and dispose of appeals against any direction issued or decision made or order passed by the Commission under sub-sections (2) and (6) of section 26, section 27, section 28, section 31, section 32, section 33, section 38, section 39, section 43, section 43A, section 44, section 45 or section 46 of the Act;
- (b) to adjudicate on claim for compensation that may arise from the findings of the Commission or the orders of the Appellate Tribunal in an appeal against any finding of the Commission or under section 42A or under sub-section(2) of section 53Q of this Act, and pass orders for the recovery of compensation under section 53N of this Act.

### **APPEAL TO APPELLATE TRIBUNAL**

The Central Government or the State Government or a local authority or enterprise or any person, aggrieved by any direction, decision or order referred to in clause (a) of section 53A may prefer an appeal to the Appellate Tribunal. Every appeal under sub-section (1) shall be filed within a period of sixty days from the date on which a copy of the direction or decision or order made by the Commission is received by the Central Government or the State Government or a local authority or enterprise or any person referred to in that sub-section and it shall be in such form and be accompanied by such fee as may be prescribed. However, the Appellate Tribunal may entertain an appeal after the expiry of the said period of sixty days if it is satisfied that there was sufficient cause for not filing it within that period.

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, confirming, modifying or setting aside the direction, decision or order appealed against. The Appellate Tribunal shall send a copy of every order made by it to the Commission and the parties to the appeal. The appeal filed before the Appellate Tribunal under sub-section (1) shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal within six months from the date of receipt of the appeal.

### **Composition of Appellate Tribunal**

The Appellate Tribunal shall consist of a Chairperson and not more than two other members to be appointed by the Central Government.

### **Qualifications for appointment of Chairperson and Members of Appellate Tribunal**

Section 53D provides that the Chairperson of the Appellate Tribunal shall be a person, who is, or has been a Judge of the Supreme Court or the Chief Justice of a High Court.

A member of the Appellate Tribunal shall be a person of ability, integrity and standing having special knowledge of, and professional experience of not less than twenty five years in, competition matters including competition law and policy, international trade, economics, business, commerce, law, finance, accountancy, management, industry, public affairs, administration or in any other matter which in the opinion of the Central Government, may be useful to the Appellate Tribunal.

### **Term of office of Chairperson and Members of Appellate Tribunal**

The Chairperson or a member of the Appellate Tribunal shall hold office as such for a term of five years from the date on which he enters upon his office, and shall be eligible for re-appointment. However, no Chairperson or other member of the Appellate Tribunal shall hold office as such after he has attained, -

- (a) in the case of the Chairperson, the age of sixty-eight years;
- (b) in the case of any other member of the Appellate Tribunal, the age of sixty-five years.

### **Resignation of Chairperson and Members of Appellate Tribunal**

The Chairperson or a member of the Appellate Tribunal may, by notice in writing under his hand addressed to the Central Government, resign his office. However, the Chairperson or a member of the Appellate Tribunal shall, unless he is permitted by the Central Government to relinquish his office sooner, continue to hold office until the expiry of three months from the date of receipt of such notice or until a person duly appointed as his successor enters upon his office or until the expiry of his term of office, whichever is the earliest.

### **Member of Appellate Tribunal to act as its Chairperson in certain cases**

In the event of the occurrence of any vacancy in the office of the Chairperson of the Appellate Tribunal by reason of his death or resignation, the senior-most Member of the Appellate Tribunal shall act as the Chairperson of the Appellate Tribunal until the date on which a new Chairperson appointed in accordance with the provisions of this Act to fill such vacancy enters upon his office.

When the Chairperson of the Appellate Tribunal is unable to discharge his functions owing to absence, illness or any other cause, the senior-most member or, as the case may be, such one of the Members of the Appellate Tribunal, as the Central Government may, by notification, authorize in this behalf, shall discharge the functions of the Chairperson until the date on which the Chairperson resumes his duties.

### **Restriction on employment of Chairperson and other Members of Appellate Tribunal in certain cases**

The Chairperson and other members of the Appellate Tribunal shall not, for a period of two years from the date on which they cease to hold office, accept any employment in, or connected with the management or administration of, any enterprise which has been a party to a proceeding before the Appellate Tribunal under the Act. However, nothing contained in this section shall apply to any employment under the Central

Government or a State Government or local authority or in any statutory authority or any corporation established by or under any Central, State or Provincial Act or a Government Company as defined in section 617 of the Companies Act, 1956.

### **Awarding compensation**

Section 53N provides that without prejudice to any other provisions contained in this Act, the Central Government or a State Government or a local authority or any enterprise or any person may make an application to the Appellate Tribunal to adjudicate on claim for compensation that may arise from the findings of the Commission or the orders of the Appellate Tribunal in an appeal against any findings of the Commission or under section 42A or under sub-section(2) of section 53Q of the Act, and to pass an order for the recovery of compensation from any enterprise for any loss or damage shown to have been suffered, by the Central Government or a State Government or a local authority or any enterprise or any person as a result of any contravention of the provisions of Chapter II, having been committed by enterprise.

Every application made under sub-section (1) shall be accompanied by the findings of the Commission, if any, and also be accompanied with such fees as may be prescribed. The Appellate Tribunal may, after an inquiry made into the allegations mentioned in the application made under sub-section (1), pass an order directing the enterprise to make payment to the applicant, of the amount determined by it as realisable from the enterprise as compensation for the loss or damage caused to the applicant as a result of any contravention of the provisions of Chapter II having been committed by such enterprise. However, the Appellate Tribunal may obtain the recommendations of the Commission before passing an order of compensation.

Where any loss or damage referred to in sub-section (1) is caused to numerous persons having the same interest, one or more of such persons may, with the permission of the Appellate Tribunal, make an application under that sub-section for and on behalf of, or for the benefit of, the persons so interested, and thereupon, the provisions of rule 8 of Order 1 of the First Schedule to the Code of Civil Procedure, 1908, shall apply subject to the modification that every reference therein to a suit or decree shall be construed as a reference to the application before the Appellate Tribunal and the order of the Appellate Tribunal thereon.

### **Procedures and powers of Appellate Tribunal**

Section 53O provides that the Appellate Tribunal shall not be bound by the procedure laid down in the Code of Civil Procedure, 1908 (5 of 1908), but shall be guided by the principles of natural justice and, subject to the other provisions of this Act and of any rules made by the Central Government, the Appellate Tribunal shall have power to regulate its own procedure including the places at which they shall have their sittings.

The Appellate Tribunal shall have, for the purposes of discharging its functions under this Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908) while trying a suit in respect of the following matters, namely:

- (a) summoning and enforcing the attendance of any person and examining him on oath;
- (b) requiring the discovery and production of documents;
- (c) receiving evidence on affidavit;
- (d) subject to the provisions of sections 123 and 124 of the Indian Evidence Act, 1872, requisitioning any public record or document or copy of such record or document from any office;
- (e) issuing commissions for the examination of witnesses or documents;
- (f) reviewing its decisions;

- (g) dismissing a representation for default or deciding it ex parte;
- (h) setting aside any order of dismissal of any representation for default or any order passed by it ex parte;
- (i) any other matter which may be prescribed.

Every proceedings before the Appellate Tribunal shall be deemed to be judicial proceedings within the meaning of sections 193 and 228, and for the purposes of section 196, of the Indian Penal Code and the Appellate Tribunal shall be deemed to be a civil court for the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

### **Execution of orders of Appellate Tribunal**

Every order made by the Appellate Tribunal shall be enforced by it in the same manner as if it were a decree made by a court in a suit pending therein, and it shall be lawful for the Appellate Tribunal to send, in case of its inability to execute such order, to the court within the local limits of whose jurisdiction,-

- (a) in the case of an order against a company, the registered office of the company is situated; or
- (b) in the case of an order against any other person, place where the person concerned voluntarily resides or carries on business or personally works for gain, is situated.

The Appellate Tribunal may transmit any order made by it to a civil court having local jurisdiction and such civil court shall execute the order as if it were a decree made by that court.

### **Contravention of orders of Appellate Tribunal**

Without prejudice to the provisions of this Act, if any person contravenes, without any reasonable ground, any order of the Appellate Tribunal, he shall be liable for a penalty of not exceeding rupees one crore or imprisonment for a term up to three years or with both as the Chief Metropolitan Magistrate, Delhi may deem fit. However, the Chief Metropolitan Magistrate, Delhi shall not take cognizance of any offence punishable under this sub-section, save on a complaint made by an officer authorized by the Appellate Tribunal.

Without prejudice to the provisions of this Act, any person may make an application to the Appellate Tribunal for an order for the recovery of compensation from any enterprise for any loss or damage shown to have been suffered, by such person as a result of the said enterprise contravening, without any reasonable ground, any order of the Appellate Tribunal or delaying in carrying out such orders of the Appellate Tribunal.

### **Right to legal representation**

A person preferring an appeal to the Appellate Tribunal may either appear in person or authorize one or more chartered accountants or company secretaries or cost accountants or legal practitioners or any of its officers to present his or its case before the Appellate Tribunal.

The Central Government or a State Government or a local authority or any enterprise preferring an appeal to the Appellate Tribunal may authorize one or more chartered accountants or company secretaries or cost accountants or legal practitioners or any of its officers to act as presenting officers and every person so authorized may present the case with respect to any appeal before the Appellate Tribunal.

The Commission may authorize one or more chartered accountants or company secretaries or cost accountants or legal practitioners or any of its officers to act as presenting officers and every person so authorized may present the case with respect to any appeal before the Appellate Tribunal.

*Explanation* – The expressions “chartered accountant” or “company secretary” or “cost accountant” or “legal practitioner” shall have the meanings respectively assigned to them in the Explanation to section 35.

### **Appeal to Supreme Court**

The Central Government or any State Government or the Commission or any statutory authority or any local authority or any enterprise or any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the Supreme Court within sixty days from the date of communication of the decision or order of the Appellate Tribunal to them. The Supreme court may, if it is satisfied that the applicant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed after the expiry of the said period of sixty days.

### **Power to Punish for contempt**

The Appellate Tribunal shall have, and exercise, the same jurisdiction, powers and authority in respect of contempt of itself as a High Court has and may exercise and, for this purpose, the provisions of the Contempt of Courts Act, 1971 (70 of 1971) shall have effect subject to modifications that,—

- (a) the reference therein to a High Court shall be construed as including a reference to the Appellate Tribunal;
- (b) the references to the Advocate-General in section 15 of the said Act shall be construed as a reference to such Law Officer as the Central Government may, by notification, specify in this behalf.

### **Miscellaneous**

#### *Power to exempt*

The Central Government may, by notification exempt from the application of the Act, or any provision thereof—

- (a) any class of enterprises if such exemption is necessary in the interest of security of the State or public interest;
- (b) any practice or agreement arising out of and in accordance with any obligation assumed by India under any treaty, agreement or convention with any other country or countries;
- (c) any enterprise, which performs a sovereign function on behalf of the Central Government or a State Government.

Thus, the power to grant exemption can be invoked by the Central Government in specified circumstances and conditions.

Where any enterprise is engaged in activities, which includes any activity relatable to the sovereign functions of the Government, exemption may be granted by the Central Government only in respect of the activity relatable to the sovereign functions.

#### *Power of Central Government to issue directions*

The Central Government may give in writing to the Commission such directions on questions of policy, other than those relating to technical and administrative matters and the Commission shall be bound by such directions. The Commission shall be given an opportunity to express its views to the Central Government before any direction is given by the Government to the Commission. The decision of the Central Government as to whether the question is of one of policy or not, shall be final.

***Power of Central Government to supersede Commission***

It is stipulated under section 56 of the Act that if at any time the Central Government is of the opinion, -

- (a) that the Commission, on account of circumstances beyond its control is unable to discharge the functions or perform the duties imposed on it by or under the provisions of the Act; or
- (b) that the commission has persistently made default in complying with any direction given by the Central Government under this Act or in discharge of functions or performance of duties imposed on it by or under the provisions of the Act and as a result of such default the financial position or the administration of the Commission has suffered; or
- (c) that the circumstances exist which render it necessary in the public interest to do so, the Central Government may, by notification and for the reasons stated therein, supersede the Commission for such period, not exceeding six months, as may be specified in the notification.

Thus, power to supersede CCI vests in the Central Government. However before issuing any such notification, the Central Government shall give to the Commission a reasonable opportunity to make representations against the proposed supersession for its consideration. Upon publication of a notification superseding the Commission—

- (a) the Chairperson and other members shall vacate the office from the date of suppression;
- (b) until Commission is reconstituted, all powers functions and duties of the Commission shall be discharged by the Central Government or by an authority specified by the Central Government in this behalf;
- (c) until the Commission is reconstituted all of its properties shall vest in the Central Government.

The Central Government shall reconstitute the Commission by a fresh appointment of its Chairman and other Members on or before the expiration of six months from the date of order of the Central Government superseding the Commission. Any Chairperson or Member who vacates the office because the Commission is unable to discharge its functions or perform duties imposed on it by or under the provisions of this Act on account of circumstance beyond its control shall not be deemed to be disqualified for re-appointment upon re-constitution of the Commission by the Government.

The Central Government shall cause a notification superseding the Commission and a full report of any action taken under this Section and circumstances leading to such action, be laid before each House of the Parliament at the earliest.

***Restriction on disclosure of information***

The Commission from time to time may require any enterprise to submit information for the purposes of the Act. The information may relate to sensitive business secrets and patents of such an enterprise. In order to ensure complete secrecy of such information, Section 57 provides that no information relating to an enterprise obtained by or on behalf of the Commission for the purposes of the Act shall be disclosed except with the previous permission of the enterprise in writing otherwise than in compliance with or for the purposes of the Act or any other law for the time being in force.

***Protection of action taken in good faith***

While acting or purporting to act in pursuance of any of the provisions of this Act, the Chairperson and other Members and the Director General, Additional, Joint, Deputy or Assistant Directors General and Registrar and officers and other employees shall be deemed to be public servants within the meaning of Section 21 of

the Indian Penal Code. However the Act provides for protection of action taken in good faith. As per Section 59 no suit or legal proceedings shall lie against the Central Government or Commission or any Chairperson or any Member or Director General or Registrar or other officers or employees of the Commission for anything, which is done or intended to be done in good faith under the Act or rules or regulations, made thereunder.

#### *Exclusion of jurisdiction of Civil Courts*

A civil court is precluded to exercise Jurisdiction in respect of any matter, which the Commission is empowered by or under the Act to determine and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under the Act.

#### *Application of other laws not barred*

The provisions of the Act are in addition to, and not in derogation of, the provisions of any other law for the time being in force.

#### **Power to make rules**

The Central Government may, by notification, make rules to carry out provisions of this Act. In particular, the Central Government may make rules to provide for all or any of the following matters; namely-

- (a) the term of the Selection Committee and the manner of selection of panel of names under sub-section (2) of Section 9;
- (b) the form and manner in which and the authority before whom the oath of office and of secrecy shall be made and subscribed to under Sub-section (3) of Section 10;
- (c) Omitted by the Competition (Amendment) Act, 2007;
- (d) the salary and the other terms and conditions of service including travelling expenses, house rent allowance and conveyance facilities, sumptuary allowance and medical facilities to be provided to the Chairperson and other Members under Sub-section (1) of Section 14;
- (da) the number of Additional, Joint, Deputy or Assistant Director General or such officers or other employees in the office of DG and the manner in which such Additional, Joint, Deputy or Assistant Director Generals or such officers or other employees may be appointed under sub-section (1A) of Section 16.
- (e) the salary, allowances and other terms and conditions of service of the Director General, Additional, Joint, Deputy or Assistant Directors General or such officers or other employees under Sub-section (3) of Section 16;
- (f) the qualifications for appointment of the Director General, Additional, Joint, Deputy or Assistant Directors General or such officers or other employees under Sub-section (4) of Section 16;
- (g) the salaries and allowances and other terms and conditions of service of the Secretary and officers and other employees payable, and the number of such officers and employees under Sub-section (2) of Section 17;
- (h) for securing any case or matter which requires to be decided by a Bench composed of more than two Members under Sub-section (4) of Section 23; (Omitted by the Competition (Amendment) Act, 2007)

- (i) any other matter in respect of which the Commission shall have power under clause (g) of Sub-section (2) of Section 36; (Omitted by the Competition (Amendment) Act, 2007)
- (j) the promotion of competition advocacy, creating awareness and imparting training about competition issues under Sub-section (3) of Section 49; (Omitted by the Competition (Amendment) Act, 2007)
- (k) the form in which the annual statement of accounts shall be prepared under Sub-section (1) of Section 52;
- (l) the time within which and the form and manner in which the Commission may furnish returns, statements & such particulars as the Central Government may require under Sub-section (1) of Section 53;
- (m) the form in which and the time within which the annual report shall be prepared under Sub-section (2) of Section 53;
- (ma) the form in which an appeal may be filed before the Appellate Tribunal under sub-section (2) of section 53B and the fees payable in respect of such appeal;
- (mb) the term of the Selection Committee and the manner of selection of panel of names under sub-section(2) of section 53E;
- (mc) the salaries and allowances and other terms and conditions of service of the Chairperson and other Members of the Appellate Tribunal under sub-section (1) of section 53G;
- (md) the salaries and allowances and other conditions of service of the officers and other employees of the Appellate Tribunal under sub-section (3) of section 53M;
- (me) the fee which shall be accompanied with every application made under sub-section (2) of section 53N;
- (mf) the other matters under clause (i) of sub-section(2) of section 53O in respect of which the Appellate Tribunal shall have powers under the Code of Civil Procedure, 1908 (5 of 1908) while trying a suit;
- (n) the manner in which the monies transferred to the Central Government shall be dealt with by that Government under the fourth proviso to Sub-section (2) of Section 66;
- (o) any other matter which is to be, or may be, prescribed, or in respect of which provision is to be, or may be, made by rules.

Every notification for making such rules shall be laid before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session, or in two or more successive sessions. If both Houses agree that notification is not be issued or rule should not be made, then rule shall not be made or if the House decides that notification or rules should have effect in such modified form then the rule or notification shall be enforced in modified form. However, any such modification or annulment shall be without prejudice to the validity of anything previously done under the notification or rule, as the case may be.

### **Power to make Regulations**

The Commission may, by notification, make regulations, which are consistent with the Act. Without prejudice to the generality of the foregoing provision, such regulations may provide for all or any of the following matters, namely, -

- (a) the cost of production to be determined under clause (b) of the Explanation to Section 4;

- (b) the form of notice as may be specified and the fee which may be determined under Sub-section (2) of Section 6;
- (c) the form in which details of acquisition shall be filed under Sub-section (5) of Section 6;
- (d) the procedure to be followed for engaging the experts and the professionals under sub-section (3) of Section 17;
- (e) the fee which may be determined under clause (a) of Sub-section (1) of Section 19;
- (f) the rules of procedure in regard to transaction of business at the meetings of the Commission under sub-section (1) of Section 22;
- (g) the manner in which penalty shall be recovered under sub-section (1) of Section 39;
- (h) any other matter in respect of which provision is to be, or may be made by regulations.

Every regulation shall be laid before both the Houses of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the regulation, or both Houses agree that the regulation should not be made, the regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be. However, any such modification or annulment shall be without prejudice to the validity of anything previously done under that regulation.

#### *Power to remove difficulties*

The Central government may, by order published in the Official Gazette, make such provisions, not inconsistent with the provisions of the Act as may appear to be necessary to remove difficulties which may arise in giving effect to the provisions of the Act. However, no such order shall be made after expiry of a period of two years from the commencement of the Act. Every order made under this Section shall be laid before both the Houses of Parliament as soon as may be, after it is made.

#### **Repeal and Saving**

Section 66 provides that the Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969) is hereby repealed and the Monopolies and Restrictive Trade Practices Commission established under sub-section (1) of section 5 of the said Act (hereinafter referred to as the repealed Act) shall stand dissolved.

(1A) The repeal of the Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969) shall, however, not affect,-

- (a) the previous operation of the Act so repealed or anything duly done or suffered thereunder; or
- (b) any right, privilege, obligation or liability acquired, accrued or incurred under the Act so repealed; or
- (c) any penalty, confiscation or punishment incurred in respect of any contravention under the Act so repealed; or
- (d) any proceeding or remedy in respect of any such right, privilege, obligation, liability, penalty, confiscation or punishment as aforesaid, and any such proceeding or remedy may be instituted, continued or enforced, and any such penalty, confiscation or punishment may be imposed or made as if that Act had not been repealed.

(2) On the dissolution of the Monopolies and Restrictive Trade Practices Commission, the person appointed as the Chairman of the Monopolies and Restrictive Trade Practices Commission and every other person

appointed as Member and Director General of Investigation and Registration, Additional, Joint, Deputy, or Assistant Directors General of Investigation and Registration and any officer and other employee of that Commission and holding office as such immediately before such dissolution shall vacate their respective offices and such Chairman and other Members shall be entitled to claim compensation not exceeding three months' pay and allowances for the premature termination of term of their office or of any contract of service:

Provided that the Director General of Investigation and Registration, Additional, Joint, Deputy or Assistant Directors General of Investigation and Registration or any officer or other employee who has been, immediately before the dissolution of the Monopolies and Restrictive Trade Practices Commission appointed on deputation basis to the Monopolies and Restrictive Trade Practices Commission, shall, on such dissolution, stand reverted to his parent cadre, Ministry or Department, as the case may be:

Provided further that the Director-General of Investigation and Registration, Additional, Joint, Deputy or Assistant Directors General of Investigation and Registration or any officer or other employee who has been, immediately before the dissolution of the Monopolies and Restrictive Trade Practices Commission, employed on regular basis by the Monopolies and Restrictive Trade Practices Commission, shall become, on and from such dissolution, the officer and employee, respectively, of the Competition Commission of India or the Appellate Tribunal, in such manner as may be specified by the Central Government, with the same rights and privileges as to pension, gratuity and other like matters as would have been admissible to him if the rights in relation to such Monopolies and Restrictive Trade Practices Commission had not been transferred to, and vested in, the Competition Commission of India or the Appellate Tribunal, as the case may be, and shall continue to do so unless and until his employment in the Competition Commission of India or the Appellate Tribunal, as the case may be, is duly terminated or until his remuneration, terms and conditions of employment are duly altered by the Competition Commission of India or the Appellate Tribunal, as the case may be.

Provided also that notwithstanding anything contained in the Industrial Disputes Act, 1947(14 of 1947), or in any other law for the time being in force, the transfer of the services of any Director General of Investigation and Registration, Additional, Joint, Deputy or Assistant Directors General of Investigation and Registration or any officer or other employee, employed in the Monopolies and Restrictive Trade Practices Commission, to the Competition Commission of India or the Appellate Tribunal, as the case may be, shall not entitle such Director General of Investigation and Registration, Additional, Joint, Deputy or Assistant Directors General of Investigation and Registration or any officer or other employee any compensation under this Act or any other law for the time being in force and no such claim shall be entertained by any court, tribunal or other authority:

Provided also that where the Monopolies and Restrictive Trade Practices Commission has established a provident fund, superannuation, welfare or other fund for the benefit of the Director General of Investigation and Registration, Additional, Joint, Deputy or Assistant Directors General of Investigation and Registration or the officers and other employees employed in the Monopolies and Restrictive Trade Practices Commission, the monies relatable to the officers and other employees whose services have been transferred by or under this Act to the Competition Commission of India or the Appellate Tribunal, as the case may be, shall, out of the monies standing on the dissolution of the Monopolies and Restrictive Trade Practices Commission to the credit of such provident fund, superannuation, welfare or other fund, stand transferred to, and vest in, the Competition Commission of India or the Appellate Tribunal as the case may be, and such monies which stand so transferred shall be dealt with by the said Commission or the Tribunal, as the case may be, in such manner as may be prescribed.

(3) All cases pertaining to monopolistic trade practices or restrictive trade practices pending (including such cases, in which any unfair trade practice has also been alleged), before the Monopolies and Restrictive

Trade Practices Commission shall, on the commencement of the Competition (Amendment) Act, 2009 stand transferred to the Appellate Tribunal and shall be adjudicated by the Appellate Tribunal in accordance with the provisions of the repealed Act as if that Act had not been repealed.

*“Explanation.—* For the removal of doubts, it is hereby declared that all cases referred to in this sub-section, sub-section (4) and subsection (5) shall be deemed to include all applications made for the losses or damages under section 12B of the Monopolies and Restrictive Trade Practices Act, 1969 as it stood before its repeal;

(4) Subject to the provisions of sub-section(3), all cases pertaining to unfair trade practices other than those referred to in clause (x) of sub-section(1) of section 36A of the Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969) and pending before the Monopolies and Restrictive Trade Practices Commission immediately before the commencement of the Competition (Amendment) Act, 2009, shall, stand transferred to the National Commission constituted under the Consumer Protection Act, 1986 (68 of 1986) and the National Commission shall dispose of such cases as if they were cases filed under that Act:

Provided that the National Commission may, if it considers appropriate, transfer any case transferred to it under this sub-section, to the concerned State Commission established under section 9 of the Consumer Protection Act, 1986 (68 of 1986) and that State Commission shall dispose of such case as if it was filed under that Act.

“Provided further that all the cases relating to the unfair trade practices pending, before the National Commission under this sub-section, on or before the date on which the Competition (Amendment) Act, 2009 receives the assent of the President, shall, on and from that date, stand transferred to the Appellate Tribunal and be adjudicated by the Appellate Tribunal in accordance with the provisions of the repealed Act as if that Act had not been repealed.”

(5) All cases pertaining to unfair trade practices referred to in clause (x) of subsection (1) of section 36A of the Monopolies and Restrictive Trade Practices Act, 1969 and pending before the Monopolies and Restrictive Trade Practices Commission shall, on the commencement of the Competition (Amendment) Act, 2009 stand transferred to the Appellate Tribunal and the Appellate Tribunal shall dispose of such cases as if they were cases filed under that Act.

(6) All investigations or proceedings, other than those relating to unfair trade practices, pending before the Director General of Investigation and Registration on or before the commencement of this Act shall, on such commencement, stand transferred to the Competition Commission of India, and the Competition Commission of India may conduct or order for conduct of such investigation or proceedings in the manner as it deems fit.

(7) All investigations or proceedings, relating to unfair trade practices, other than those referred to in clause (x) of sub-section (1) of section 36A of the Monopolies and Restrictive Trade Practices Act, 1969(54 of 1969) and pending before the Director General of Investigation and Registration on or before the commencement of this Act shall, on such commencement, stand transferred to the National Commission constituted under the Consumer Protection Act, 1986 (68 of 1986) and the National Commission may conduct or order for conduct of such investigation or proceedings in the manner as it deems fit.

“Provided that all investigations or proceedings, relating to unfair trade practices pending before the National Commission, on or before the date on which the Competition (Amendment) Bill, 2009 receives the assent of the President shall, on and from that date, stand transferred to the Appellate Tribunal and the Appellate Tribunal may conduct or order for conduct of such investigation or proceedings in the manner as it deems fit.”

(8) All investigations or proceedings relating to unfair trade practices referred to in clause (x) of subsection (1) of section 36A of the Monopolies and Restrictive Trade Practices Act, 1969(54 of 1969), and pending

before the Director General of Investigation and Registration on or before the commencement of this Act shall, on such commencement, stand transferred to the Competition Commission of India and the Competition Commission of India may conduct or order for conduct of such investigation in the manner as it deems fit.

(9) Save as otherwise provided under sub-sections (3) to (8), all cases or proceedings pending before the Monopolies and Restrictive Trade Practices Commission shall abate.

(10) The mention of the particular matters referred to in sub-sections (3) to (8) shall not be held to prejudice or affect the general application of section 6 of the General Clauses Act, 1897 (10 of 1897) with regard to the effect of repeal.

### LESSON ROUND UP

- Competition Act, 2002 seeks to provide, keeping in view the economic development of the country, for the establishment of Competition Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interests of consumers and to ensure freedom of trade carried on by other participants in markets in India and for matters connected therewith or incidental thereto besides repeal of MRTP Act and the dissolution of the MRTP Commission.
- No enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition.
- Competition Act expressly prohibits any enterprise or group from abusing its dominant position. Dominant Position meaning thereby a position of strength, enjoyed by an enterprise or group, in the relevant market, in India, which enables it to operate independently of competitive forces prevailing in the relevant market; or affect its competitors or consumers or the relevant market in its favour.
- Competition Act prohibits any person or enterprise from entering into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and if such a combination is formed it shall be void.
- While formulating a policy on the competition the Central/State Government may make a reference to the Commission for its opinion on possible effect of such a policy on the competition.
- Competition Appellate Tribunal to hear and dispose of appeals against the direction issued or decision made or orders passed by the Commission under the Act, and to adjudicate on claim of compensation.
- The Central Government or any State Government or the Commission or any statutory authority or any local authority or any enterprise or any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the Supreme.

### SELF TEST QUESTIONS

1. Define and discuss the Relevant Market, Relevant Geographic Market, and Relevant Product Market.
2. What are anti-competitive agreements. Discuss the procedure for enquiry into anti-competitive agreements.
3. Discuss the composition and functions of Competition Commission of India.
4. The Competition Act does not prohibit dominance, but the abuse of dominant position. Explain.
5. Write short notes on:
  - (i) Combinations.
  - (ii) Competition Advocacy.



# CONSUMER PROTECTION – LAW AND PRACTISE

## Section II

### LESSON OUTLINE

- Genesis of Consumer Protection Laws
- Object and scope of the Consumer Protection Act, 1986
- Consumer Rights
- Meaning of Consumer
- Commercial purpose
- Defect in Goods
- Deficiency in Service
- Contract of Service
- Contract for Service
- District Forum
- State Consumer Protection Council
- Central Consumer Protection Council
- Jurisdiction of Protection Council
- Transfer of Cases
- Limitation Period for Filing Complaint
- Administrative Control
- Appeal
- Nature and Scope of Remedies
- Offences and Penalty

### LEARNING OBJECTIVES

Every individual is a consumer, regardless of occupation, age, gender, community, cast, creed, religion or race. Consumer rights and welfare are an integral part of the life of an individual and we all have made use of them at some or the other point in our daily routine. Consumer is the real deciding factor for all economic activities. It is now universally accepted that the extent of consumer protection is a true indicator of the level of progress in a nation. Taking into account the interests and needs of consumers in all countries, particularly those in developing countries, recognizing that consumers often face imbalances in economic terms, educational level and bargaining power, and bearing in mind that consumer should have the right of access to non-hazardous products, as well as importance of promoting just, equitable and sustainable economic and social development, the Secretary General, United Nations submitted draft guidelines for consumer protection to the Economic and Social Council in 1983. Thereupon on an extensive discussions and negotiations among various countries on the scope and content of such impending legislation certain guidelines were arrived at.

In line with the international development on consumer protection, the Parliament enacted Consumer Protection Act, 1986 provides a forum for speedy and simple redressal of consumer disputes. The rights under the consumer protection flow from the rights enshrined in Articles 14 to 19 of the Constitution of India.

According to the preamble, the Consumer Protection Act, 1986 to provide for better protection of the interests of consumers and for that purpose to make provision for the establishment of consumer councils and other authorities for the settlement of consumers disputes and for matters connected therewith.

## INTRODUCTION

A consumer is a user of goods and services, therefore, every producer is also a consumer. However, conflicting interests have categorised them, inevitably, into two different groups. The industrial revolution brought in the concept of standardisation and mass production and over the years, the type of goods and the nature of services available grew manifold. The doctrine of 'Caveat Emptor' or 'let the buyer beware' which came into existence in the middle ages had been replaced by the principle of 'Consumer Sovereignty' or 'Consumer is the King'. But, with tremendous increase in the world population, the growing markets were unable to meet the rising demand which created a gap between the general 'demand' and 'supply' levels in the markets. This to some extent watered down the concept of 'Consumer Sovereignty', what with consumers being forced to accept whatever was offered to them. On the other hand, the expanding markets necessitated the introduction of various intermediaries between the producer and the ultimate consumer. 'Advertising', though ostensibly directed at informing potential consumers about the availability and uses of a product began to be resorted to as a medium for exaggerating the uses of ones products or disparaging others products so as to have an edge over competitors. Unfair and deceptive practices such as selling of defective or sub-standard goods, charging exorbitant prices, misrepresenting the efficacy or usefulness of goods, negligence as to safety standards, etc. became rampant. It, therefore, became necessary to evolve statutory measures, even in developed countries, to make producers/traders more accountable to consumers. It also became inevitable for consumers to unite on a common platform to deal with issues of common concern and having their grievances redressed satisfactorily.

### Genesis of Consumer Protection Laws

The need to ensure the basic rights to health, safety, etc. of consumers has long been recognised the worldover and various general legislations were enacted in India and abroad in this direction. In India, the general enactments other than the law of torts which ultimately aimed at protection of consumers interests are the Indian Contract Act, 1872, the Sale of Goods Act, 1930, the Dangerous Drugs Act, 1930, the Agricultural Produce (Grading and Marketing) Act, 1937, the Drugs and Cosmetics Act, 1940, the Indian Standards Institution (Certification Marks) Act, 1952, the Prevention of Food Adulteration Act, 1954, the Drugs and Magic Remedies (Objectionable Advertisements) Act, 1954, the Essential Commodities Act, 1955, the Standards of Weights and Measures Act, 1976 (Now Legal Metrology Act, 2009), the Trade and Merchandise Marks Act, 1958, (Now Trade Marks Act, 1999), the Patents Act, 1970, the Hire Purchases Act, 1972 and the Prevention of Black Marketing and Maintenance of Supplies of Essential Commodities Act, 1980.

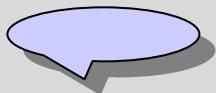
These legislations contained regulatory provisions and contravention of these provisions attracted civil liability. This meant that an ordinary consumer had no other remedy but to initiate action by way of a civil suit which involved lengthy legal process proving to be too expensive and time consuming for lay consumers. In fact, at times, the time and cost involved in the legal process was disproportionate to the compensation claimed and granted to an individual consumer. Though the MRTP Commission proved to be far more accessible and less time-consuming than the Civil Courts, its single central location at New Delhi did not make the redressal agency accessible to all consumers, especially those located in the remote towns and villages of the country. Therefore, it became necessary to evolve laws directed at protecting the consumers and at the same time, providing for remedies which are simpler, more accessible, quicker and less expensive.

This paved the way for enactment of the Consumer Protection Act in 1986 providing for simple, quick and easy remedy to consumers under a three-tier quasi-judicial redressal agency at the District, State and

National levels. To make the Act more effective and meaningful, necessary changes have been brought by Consumer Protection (Amendment) Act, 2002, which came into force w.e.f. March 15, 2003.

### The Basic Rights of Consumers

***The basic rights of consumers that are sought to be promoted and protected are:***



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

This is based on the basic rights of consumers as defined by the International Organisation of Consumers (IOCU) viz., the Rights to Safety, to Information, of Choice, to be Heard, to Redressal, to Consumer Education, to Healthy Environment and to Basic Needs.

### Scope of the Act

The Act extends to the whole of India except the State of Jammu and Kashmir and applies to all goods and services unless otherwise notified by the Central Government. The Act received the Presidents assent on 24.12.1986. However, all provisions of the Act except those relating to establishment, composition, jurisdiction, etc. of the Consumer Disputes Agencies (which came into force on 1.7.1987) came into force on 15.4.1987.

### DEFINITIONS

Section 2(1) of the Act defines various terms used in the Act. Some of the definitions are given hereunder:

#### ***Complainant means***

- (i) a consumer, or
  - (ii) any voluntary consumer association registered under the Companies Act, 1956, or under any other law for the time being in force; or
  - (iii) the Central Government or any State Government, who or which makes a complaint; or
  - (iv) one or more consumers where there are numerous consumers having the same interest;
  - (v) in case of death of a consumer, his legal heir or representative;
- who or which makes a complaint [Section 2(1)(b)]

An association of persons, to have *locus standi* as consumer, it is necessary that all the individual persons forming the association must be consumers under Section 2(1)(d) of the Act having purchased the same goods/hired the same service from the same party i.e. they should have a common cause of action. Thus, unlike MRTP Act, 1969, the Redressal Machinery under Consumer Protection Act, 1986 has no power to initiate cases *suo-moto*.

**Complaint** means any allegation in writing made, with a view to obtaining any relief, by a complainant that

- (i) an unfair trade practice or a restrictive trade practice has been adopted by any trader or service provider;
- (ii) the goods bought by him or agreed to be bought by him suffer from one or more defects;
- (iii) the services hired or availed of or agreed to be hired or availed of by him suffer from deficiency in any respect;
- (iv) a trader or the service provider, as the case may be, has charged for the goods or for the services mentioned in the complaint, a price in excess of the price—
  - fixed by or under any law for the time being in force;
  - displayed on the goods or any package containing such goods;
  - displayed on the price list exhibited by him by or under any law for the time being in force
  - agreed between the parties.
- (v) goods which will be hazardous to life and safety when used are being offered for sale to the public,—
  - in contravention of any standards relating to safety of such goods as required to be complied with, by or under any law for the time being in force;
  - if the trader could have known with due diligence that the goods so offered are unsafe to the public.
- (vi) services which are hazardous or likely to be hazardous to life and safety of the public when used, are being offered by the service provider which such person could have known with due diligence to be injurious to life and safety. [Section 2(1)(c)].

**Consumer** means any person who

- (a) 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 or promised or partly paid or partly promised, or under any system of deferred payment 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
- (b) hires or avails of any services 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 beneficiary of such services other than the person who hires or avails of the services for consideration paid or promised, or partly paid and partly promised, or under any system of deferred payment, when such services are availed of with the approval of the first mentioned person but does not include a person who avails of such services for any commercial purpose. [Section 2(1)(d)].



It has been clarified that the term commercial purpose does not include use by a consumer of goods bought and used by him exclusively for the purpose of earning his livelihood by means of self-employment.

Therefore, to be a 'consumer' under the Act:

- (i) the goods or services must have been purchased or hired or availed of for consideration which has been paid in full or in part or under any system of deferred payment, i.e. in respect of hire purchase transactions;
- (ii) goods purchased should not be meant for re-sale or for a commercial purpose. Goods purchased by a dealer in the ordinary course of his business and those which are in the course of his business to supply would be deemed to be for 're-sale'; and
- (iii) in addition to the purchaser(s) of goods, or hirer(s) or users of services, any beneficiary of such services, using the goods/services with the approval of the purchaser or hirer or user would also be deemed a 'consumer' under the Act.

A purchase of goods can be said to be for a 'commercial purpose' only if the goods have been purchased for being used in some profit making activity on a large-scale, and there is close and direct nexus between the purchase of goods and the profit-making activity. *In Laxmi Engineering Works v. P.S.G. Industrial Institute, Supreme Court* held that the explanation to Section 2(1)(d) is clarificatory in nature. It observed that whether the purpose for which a person has bought goods is a 'commercial purpose' is always a question of facts and to be decided in the facts and circumstances of each case. If the commercial use is by the purchaser himself for the purpose of earning his livelihood by means of self employment such purchaser of goods would yet be a consumer. The Supreme Court further observed that if a person purchased a machine to operate it himself for earning his livelihood, he would be a consumer. If such person took the assistance of one or two persons to assist him in operating the machine, he would still be a consumer. But if a person purchases a machine and appoint or engage another person exclusively to operate the machine, then such person would not be a consumer.

*In Bhupendra Jang Bahadur Guna v. Regional Manager and Others* (II 1995 CPJ 139), the National Commission held that a tractor purchased primarily to till the land of the purchaser and let out on hire during the idle time to till the lands of others would not amount to commercial use.

The question as to whether the widow of the deceased policy holder was a 'consumer' under the Act was decided in the affirmative by the State Commission in Andhra Pradesh in the case of *A Narasamma v. LIC of India*. The State Commission held that as the term 'consumer' includes any beneficiary of service other than the person who hires the services for consideration, the widow being the beneficiary of services is a 'consumer' under the Act entitled to be compensated for the loss suffered by her due to negligence of the LIC.

*In Laxmiben Laxmichand Shah v. Sakerben Kanji Chandan and others* 2001 CTJ 401 (Supreme Court) (CP), the Supreme Court held that the tenant entering into lease agreement with the landlord cannot be considered as consumer under Section 2(1)(d) of the Act. Where there was no provision in the lease agreement in respect of cleaning, repairing and maintaining the building, the rent paid by tenant is not the consideration for availing these services and therefore, no question of deficiency in service.

**Goods**, in terms of Section 2(1)(i) has been defined to mean goods as defined in the Sale of Goods Act, 1930. As per Section 2(7) of the Sale of Goods Act, 1930 Goods means every kind of movable property

other than actionable claims and money; and includes stock and shares, growing crops, grass and things attached to or forming part of the land, which are agreed to be severed before sale or under the contract of sale. Therefore, most consumer products come under the purview of this definition.

*In Morgan Stanley Mutual Fund v. Kartik Das (1994) 3 CLJ 27*, the Supreme Court held that an application for allotment of shares cannot constitute goods. It is after allotment, rights may arise as per the articles of association of the company. At the stage of application there is no purchase of goods for consideration and again the purchaser cannot be called the hirer of services for consideration.

**Service** :The term 'service' is defined under Section 2(1)(o) as to mean service of any description which is made available to potential users and includes, but not limited to the provision of facilities in connection with banking, financing, insurance, transport, processing, supply of electrical or other energy, board or lodging or both, housing construction, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service.

Passengers travelling by trains on payment of the stipulated fare charged for the ticket are 'consumers' and the facility of transportation by rail provided by the railway administration is a 'service' rendered for consideration as defined in the Act Subscribers of telephones would also be 'consumer' under the Act.

### Contract of Service and Contract for Service



*The Supreme Court in the case of Indian Merchants Association v. V P Santha, (CA No. 688 of 1993 decided on 13th November 1995) observed that a contract for service implies a contract whereby one party undertakes to render services e.g. professional or technical services to or for another in the performance of which he is not subject to detailed direction and control but exercises professional or technical skill and uses his own knowledge and discretion. A contract of service on the other hand implies relationship of master and servant and involves an obligation to obey orders in the work to be performed and as to its mode and manner of performance. The Parliamentary draftsman was well aware of this well-accepted distinction between 'contract of service' and 'contract for services' and had deliberately chosen the expression 'contract of service' instead of the expression 'contract for service' in the exclusionary part of the definition of 'service', this being the reason being that an employer could not be regarded as a consumer in respect of the services rendered by his employee in pursuance of contract of employment. By affixing the adjective 'personal' to the word 'service' the nature of the contracts which were excluded were not altered. The adjective only emphasised that what was sought to be excluded was personal service only. The expression contract of personal service in the exclusionary part of Section 2(1)(o) must, therefore, be construed as excluding the services rendered by an employee to his employer under the contract of personal service free from the ambit of the expression service.*

**Service Rendered under Medicare Insurance Scheme:** Service rendered by a medical practitioner or hospital/nursing home can not be regarded as service rendered free of charge, if the person availing the service has taken an insurance policy for medical care whereunder the charges for consultation, diagnosis and medical treatment are borne by the insurance company and such service would fall within the ambit of 'service' as defined in Section 2(1)(o). Similarly, where as a part of the conditions of service, the employer bears the expenses of medical treatment of an employee and his family members dependent on him, service rendered to such an employee and his family members would not be free of charge and would constitute 'service' under Section 2(1)(o) of the Act.

*In State of Haryana v. Santra* [2000(3) SCALE 417], the Supreme Court held that in a country where the population has been increasing rapidly and the Government has taken up the family planning as an important programme, the medical officer as also the State Government must be held responsible in damages if the family planning operation is a failure on account of the medical officers negligence because this has created additional burden on the parents of the child.

*In the case of Alex J. Rebello v. Vice Chancellor, Bangalore University and others*, 2003 CTJ 575 (CP) (NCDRC) the National Commission has held that the University in conducting examination, evaluating answer sheets and publishing the result was not performing any service for consideration and a candidate who appeared for the examination cannot be regarded as a consumer.

**Consumer Dispute** means a dispute where the person against whom a complaint has been made, denies or disputes the allegation contained in the complaint [Section 2(1)(e)].

**Restrictive Trade Practice** means a trade practice which tends to bring about manipulation of price or its conditions of delivery or to affect flow of supplies in the market relating to goods or services in such a manner as to impose on the consumers unjustified costs or restrictions and shall include—

- (a) delay beyond the period agreed to by a trader in supply of such goods or in providing the services which has led or is likely to lead to rise in the price;
- (b) any trade practice which requires a consumer to buy, hire or avail of any goods or, as the case may be, services as condition precedent to buying, hiring or availing of other goods or services.[Section 2(1)(nn)].

**Defect** means any fault, imperfection or shortcoming in the quality, quantity, potency, purity or standard which is required to be maintained by or under any law for the time being in force or under any contract, express or implied, or as is claimed by the trader in any manner whatsoever in relation to any goods [Section 2(1)(f)].

It is clear from the above definition that non-fulfilment of any of the standards or requirements laid down under any law for the time being in force or as claimed by the trader in relation to any goods fall under the ambit of defect. Therefore, contravention of any of the provisions of enactments such as the Drugs & Cosmetics Act, 1950, , the Prevention of Food Adulteration Act, 1955, the Indian Standards Institution (Certification Marks) Act, 1952 etc. or any rules framed under any such enactment or contravention of the conditions or implied warranties under the Sale of Goods Act, 1930 in relation to any goods have also been treated as a defect under the Act. Fault, imperfection or shortcoming in quality, quantity, potency, purity or standard as claimed by the trader in any manner whatsoever in relation to goods is to be determined with reference to the warranties or guarantees expressly given by a trader.

**Deficiency** means any fault, imperfection, shortcoming or inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law for the time being in force or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to any service [Section 2(1)(g)].

Failure to maintain the quality of performance required by the law or failure to provide services as per warranties given, by the provider of the service would amount to 'deficiency'.

*In Divisional Manager, LIC of India v. Bhavanam Srinivas Reddy*, the National Commission observed that default or negligence in regard to settlement of an insurance claim (on allegation of suppression of material facts, in this particular case) would constitute a deficiency in service on the part of the insurance company

and it will be perfectly open for the aggrieved consumer to approach the Redressal Forums to seek appropriate relief.

*In Jaipur Metals and Electrical Ltd. v. Laxmi Industries*, the National Commission held that a reading of Section 2(1)(g) of the Act shows that deficiency must pertain to the 'performance' in terms of quality, nature and manner to be maintained or had been undertaken to be performed in pursuance of a contract.

*In Punjab National Bank v. K.B. Shetty* (First Appeal No. 7 of 1991 decided on 6th August, 1991), ornaments kept in the banks locker were found lost though the certificate recorded by the custodian of the bank on the day the customer operated the locker stated that all lockers operated during the day have been checked and found properly locked. The National Commission upholding the decision of the State Commission, held the bank guilty of negligence and therefore, liable to make good the loss.

However, failure to provide nursing and financing facilities to a small scale industry which consequently became sick cannot be said to constitute 'deficiency in service' as in matters of grant or withholding of further advances and insisting on margin money, banks may exercise their discretion and act in accordance with their best judgement after taking into account various relevant factors. Therefore, the proper forum to agitate such grievances is a civil court (*Special Machines v. Punjab National Bank*, Original Petition No. 32/1989 decided on 22.12.1989; *M.L. Joseph v. SBI*: O.P. No. 2/1989 decided on 31.8.1989). It has also been held by National Commission in the case of *Mrs. Anumati v. Punjab National Bank* (2003 CTJ 921 (CP) (NCDRC) that the financial institutions have every right to protect their interests by taking conscious decisions. There shall be no deficiency in service where the bank takes conscious decision to adjust the fixed deposit of the joint holders against the loan taken by a third party when the FDR has been mortgaged as guarantee for loan.

Failure of a Housing Board to give possession of the flat after receiving the price and after registering it in favour of the allottee was held to be 'deficiency in service' in the case of *Lucknow Development Authority v. Roop Kishore Tandon* F.N. No. 54/1990 decided on 10.10.1990.

Cancellation of train services by the railways due to disturbance involving violence so as to safeguard the passengers as well as its own property was held by the National Commission as not constituting 'deficiency in service' on the part of the Railway. [*Dainik Rail Yatri Sangh (Regd.) v. The General Manager, Northern Railway - I* (1992) CPJ 218 (NC)]. Failure of the Railways to provide cushioned seats in the first class compartments as per specifications laid down by the Railway Board and to check unauthorised persons from entering and occupying first class compartments was held to be 'deficiency' [*N. Prabhakaran v. General Manager, Southern Railway, Madras - I* (1992) CPJ 323 (NC)].

*In Union Bank of India v. Seppo Rally OY* (1999) 35 CLA 203, the Supreme Court held that delay in payment of an unconditionally guaranteed amount by a bank in India to a non-resident in Finland in foreign currency can not be attributed to any deficiency in the service of the bank when the banks stand is that the delay is caused by the failure of a bank in Finland, to which the remittance was to have been made under the non-residents instructions to reply to the Indian Banks valid query in this connection and the RBI took time to grant the necessary permission to make the remittance.

## CONSUMER PROTECTION COUNCILS

The interests of consumers are sought to be promoted and protected under the Act inter alia by establishment of Consumer Protection Councils at the Central, State and District Levels. Chapter II of the Consumer Protection Act, 1986 comprising Sections 4 to 8 deals with Consumer Protection Councils.

### **Central Consumer Protection Council**

Section 4 empowers the Central Government to establish a Council to be known as the Central Consumer Protection Council (hereinafter referred to as the Central Council), consisting of the Minister in charge of Consumer Affairs in the Central Government, as its Chairman, and such number of other official or non-official members representing such interests as may be prescribed. However, the Consumer Protection Rules, 1987 restrict the number of members of the Central Council to 150 members.

Section 5 of the Act requires the Central Council to meet as and when necessary, but atleast once in every year. The procedure in regard to transaction of its business at the meeting is given in Rule 4 of the Rules.

### **State Consumer Protection Council**

Section 7 provides for the establishment of State Consumer Protection Councils by any State Government (by notification) to be known as Consumer Protection Council for (name of the State). The State Council shall consist of a Minister incharge of Consumer Affairs in the State Government as its Chairman and such number of other official or non-official members representing such interests as may be prescribed by the State Government and 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 procedure to be observed in regard to the transaction of its business at such meetings shall be prescribed by the State Government.

### **District Consumer Protection Council**

In order to promote and protect the rights of the consumers within the district, section 8A provides for establishment in every district of a council to be known as the District Consumer Protection Council .It shall consist of the Collector of the district (by whatever name called), who shall be its Chairman and such number of other official and non-official members representing such interests as may be prescribed by the State Government. 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 Chairman may think fit and shall observe such procedure in regard to the transaction of its business as may be prescribed by the State Government.

### **REDRESSAL MACHINERY UNDER THE ACT**

The Act provides for a three-tier quasi-judicial redressal machinery at the District, State and National level for redressal of consumer disputes and grievances. The District Forum has jurisdiction to entertain complaints where the value of goods/services complained against and the compensation, if any claimed, does not exceed Rs.20 lakhs, the State Commission for claims exceeding Rs. 20 lakhs but not exceeding Rs. 1 crore; and the National Commission for claims exceeding Rs.1 crore.

### **District Forum**

Section 9 of the Act provides for the establishment of a District Forum by the State Government in each district of the State. However, the State Government may establish more than one District Forum in a district if it deems fit to do so. Section 10(1) provides that each District Forum shall consist of:

- (a) a person who is, or who has been, or is qualified to be, a District Judge, who shall be its President;
- (b) two other members one of whom shall be a woman, who shall have the following qualifications,

namely:

- (i) be not less than thirty-five years of age,
- (ii) possess a bachelor's degree from a recognised university,
- (iii) be persons of ability, integrity and standing, and have adequate knowledge and experience of at least ten years in dealing with problems relating to economics, law, commerce, accountancy, industry, public affairs or administration:

Provided that a person shall be disqualified for appointment as a member if he—

- (a) has been convicted and sentenced to imprisonment for an offence, which, in the opinion of the State Government involves moral turpitude; or
- (b) is an undischarged insolvent; or
- (c) is of unsound mind and stands so declared by a competent court; or
- (d) has been removed or dismissed from the service of the Government or a body corporate owned or controlled by the Government; or
- (e) has, in the opinion of the State Government, such financial or other interest as is likely to affect prejudicially the discharge by him of his functions as a member; or
- (f) has such other disqualification as may be prescribed by the State Government.

Every member of the District Forum shall hold office for a term of 5 years or upto the age of 65 years, whichever is earlier, and shall be eligible for reappointment for another term of five years or upto the age of sixty-five years, whichever is earlier, subject to the condition that he fulfills the qualifications and other conditions for appointment mentioned in Section 10(1)(b) and such re-appointment is also made on the basis of the recommendation of the Selection Committee. A member may resign his office in writing under his hand addressed to the State Government.

### **Jurisdiction of District Forum**

Section 11 provides for the jurisdiction of the District Forum under two criteria pecuniary and territorial.

#### **Pecuniary limits**

Section 11(1) empowers the District Forum to entertain complaints where the value of goods or services and the compensation, if any, claimed does not exceed rupees twenty lakhs.

#### **Territorial limits**

Section 11(2) requires a complaint to be instituted in the District Forum within the local limits of whose jurisdiction the opposite party or the defendant actually and voluntarily resides or carries on business or has a branch office or personally works for gain, at the time of institution of the complaint; or any one of the opposite parties (where there are more than one) actually and voluntarily resides or carries on business or has a branch office or personally works for gain, at the time of institution of the complaint, provided that the other opposite party/parties acquiesce in such institution or the permission of the Forum is obtained in respect of such opposite parties; or the cause of action arises, wholly or in part.

*In the case of Dynavox Electronic Pvt. Ltd. v. B.J.S. Rampuria Jain College, Bikaner* (Appeal No. 4/89 before the Rajasthan CDRC), it was held that where in a contract, the machinery was supplied and installed at a particular place, a part of cause of action would be deemed to have arisen at that place, therefore, the complaint could be instituted in the District Forum within whose jurisdiction that place falls.

### State Commission

Section 16 of the Act empowers the State Government to establish the State Consumer Disputes Redressal Commission consisting of:

- (a) a person who is or has been a judge of a High Court appointed by the State Government (in consultation with the Chief Justice of the High Court) who shall be its President.
- (b) not less than two and not more than such number of members, as may be prescribed, one of whom shall be a woman, who shall have the following qualifications, namely:
  - (i) be not less than thirty-five years of age,
  - (ii) possess a bachelor's degree from a recognised university, and
  - (iii) be persons of ability, integrity and standing, and have adequate knowledge and experience of at least ten years in dealing with problems relating to economics, law, commerce, accountancy, industry, public affairs or administration:

It is required that not more than fifty per cent of the members be from amongst persons having a judicial background. "Persons having judicial background" shall mean persons having knowledge and experience for at least a period of ten years as a presiding officer at the district level court or any tribunal at equivalent level.

A person shall be disqualified for appointment as a member if he—

- (a) has been convicted and sentenced to imprisonment for an offence, which, in the opinion of the State Government involves moral turpitude; or
- (b) is an undischarged insolvent; or
- (c) is of unsound mind and stands so declared by a competent court; or
- (d) has been removed or dismissed from the service of the Government or a body corporate owned or controlled by the Government; or
- (e) has in the opinion of the State Government, such financial or other interest, as is likely to affect prejudicially the discharge by him of his functions as a member; or
- (f) has such other disqualification as may be prescribed by the State Government.

Every appointment shall be made by the State Government on the recommendation of a Selection Committee consisting of the President of the State Commission, Secretary Law Department of the State and Secretary in charge of Consumer Affairs in the State. The proviso to this clause states that where the President of the State Commission is, by reason of absence or otherwise, unable to act as Chairman of the Selection Committee, the State Government may refer the matter to the Chief Justice of the High Court for nominating a sitting Judge of that High Court to act as Chairman. Section 16(2) empowers the State Government to decide on the salary or honorarium and other allowances payable to the members of the State Commission and the other terms and conditions of service.

Every member of the State Commission shall hold office for a term of five years or upto the age of sixty-seven years, whichever is earlier and shall be eligible for reappointment for another term of five years or upto the age of sixty-seven years, whichever is earlier, subject to the condition that he fulfills the qualifications and other conditions for appointment mentioned in Section 16(1)(b) and such re-appointment is made on the basis of the recommendation of the Selection Committee.

## Jurisdiction of State Commission

Section 17 of the Act provides for the jurisdiction of the Commission as follows:

- (a) the State Commission can entertain complaints where the value of the goods or services and the compensation, if any claimed exceed rupees twenty lakhs but does not exceed rupees one crore;
- (b) the State Commission also has the jurisdiction to entertain appeals against the orders of any District Forum within the State. However, under second proviso to Section 15 no appeal by a person, who is required to pay any amount in terms of an order of the District Forum, shall be entertained by the State Commission unless the appellant has deposited in the prescribed manner fifty percent of the amount or rupees twenty-five thousand, whichever is less;
- (c) the State Commission also has the power to call for the records and pass appropriate orders in any consumer dispute which is pending before or has been decided by any District Forum within the State, if it appears to it that such District Forum has exercised any power not vested in it by law or has failed to exercise a power rightfully vested in it by law or has acted illegally or with material irregularity.

A complaint shall be instituted in a State Commission within the limits of whose jurisdiction, -

- (a) the opposite party or each of the opposite parties, where there are more than one, at the time of the institution of the complaint, actually and voluntarily resides or carries on business or has a branch office or personally works for gain; or
- (b) any of the opposite parties, where there are more than one, at the time of the institution of the complaint, actually and voluntarily resides, or carries on business or has a branch office or personally works for gain, provided that in such case either the permission of the State Commission is given or the opposite parties who do not reside or carry on business or have a branch office or personally work for gain, as the case may be, acquiesce in such institution; or
- (c) the cause of action, wholly or in part, arises

*The State Commission's jurisdiction may be original, appellate or revisional. In respect of (c) above, the State Commission may reverse the orders passed by the District Forum on any question of fact or law or correct any error of fact or of law made by the Forum.*

The National Commission in *Indian Airlines v. Consumer Education and Research Society* (1992) CPR 4 (NC) held that in respect of the original jurisdiction of the State Commission, Section 17 only prescribes pecuniary limits. No territorial limits have been fixed for the exercise of original jurisdiction under the Act though the provision contained in Section 11(2) of the Act apply *mutatis mutandis* in the matter of entertaining original complaints by the State Commission. The territorial jurisdiction of the State Commission therefore extends to the territorial limit of the State. In the exercise of its appellate jurisdiction, the State Commission may entertain appeals only against the orders of any District Forum within the State. Similar condition also applies in respect of the State Commissions power to revise orders of the District Forums - only orders of the District Forum within the State may be subject to revision by the State Commission.

## Transfer of Cases

Section 17A empowers the State Commission on the application of the complainant or of its own motion to

transfer, at any stage of the proceeding any complaint pending before the District Forum to another District Forum within the State if the interest of justice so requires.

### **National Commission**

Section 9 empowers the Central Government to establish the National Consumer Disputes Redressal Commission, by notification in the Official Gazette. Section 20(1) provides that the National Commission shall consist of—

- (a) a person who is or has been a judge of the Supreme Court, to be appointed by the Central Government (in consultation with the Chief Justice of India), who shall be its President;
- (b) not less than four and not more than such number of members as may be prescribed one of whom shall be a woman, who shall have the following qualifications, namely:-
  - (i) be not less than thirty-five years of age;
  - (ii) possess a bachelor's degree from a recognized university; and
  - (iii) be persons of ability, integrity and standing and have adequate knowledge and experience of at least ten years in dealing with problems relating to economics, law, commerce, accountancy, industry, public affairs or administration:

Provided that not more than fifty percent of the members shall be from amongst the persons having judicial background. "Persons having judicial background" shall mean persons having knowledge and experience for at least a period of ten years as a presiding officer at the district level court or any tribunal at equivalent level:

A person shall be disqualified for appointment if he—

- (a) has been convicted and sentenced to imprisonment for an offence, which, in the opinion of the Central Government involves moral turpitude; or
- (b) is an undischarged insolvent; or
- (c) is of unsound mind and stands so declared by a competent court; or
- (d) has been removed or dismissed from the service of the Government or a body corporate owned or controlled by the Government; or
- (e) has in the opinion of the Central Government such financial or other interest as is likely to affect prejudicially the discharge by him of his functions as a member; or
- (f) has such other disqualification as may be prescribed by the Central Government

Every appointment by the Central Government is required to be made on the recommendation of a Selection Committee consisting of a Judge of the Supreme Court to be nominated by the Chief Justice of India, the Secretary in the Department of Legal Affairs and the Secretary in charge of Consumer Affairs in the Government of India. Section 20(2) empowers the Central Government to fix the salary/ honorarium and other allowances payable to the members as well as the other terms and conditions of their service. Every member of the National Commission shall hold office for a term of five years or upto seventy years of age, whichever is earlier and shall be eligible for reappointment for another term of five years or upto the age of seventy years, whichever is earlier, subject to the condition that he fulfills the qualifications and other conditions for appointment mentioned in Section 20(1)(b) and such re-appointment is made on the basis of the recommendation of the Selection Committee.

## Jurisdiction of National Commission

Section 21 provides that the National Commission shall have jurisdiction:

- (a) to entertain complaints where the value of the goods or services and the compensation, if any, claimed exceeds rupees one crore;
- (b) to entertain appeals against the orders of any State Commission. However, under second proviso to Section 19 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 in the prescribed manner fifty percent of the amount or rupees thirty-five thousands, whichever is less; and
- (c) to call for the records and pass appropriate orders in any consumer dispute which is pending before, or has been decided by any State Commission where it appears to the National Commission that such State Commission has exercised a jurisdiction not vested in it by law, or has failed to exercise a jurisdiction so vested, or has acted in the exercise of its jurisdiction illegally or with material irregularity.

## Complaints before the District Forum and State Commission

Section 12 provides that a complaint, in relation to any goods sold or delivered or agreed to be sold or delivered or any service provided or agreed to be provided may be filed with the District Forum by—

- (a) the consumer to whom such goods are sold or delivered or agreed to be sold or delivered or such service provided or agreed to be provided;
- (b) any recognised consumer association, whether the consumer to whom the goods sold or delivered or agreed to be sold or delivered or service provided or agreed to be provided, is a member of such association or not; or
- (c) one or more consumers, where there are numerous consumers having the same interest with the permission of the District Forum, on behalf of, or for the benefit of, all consumers so interested; or
- (d) the Central or the State Government as the case may be, either in its individual capacity or as a representative of interests of the consumers in general.

Every complaint filed under this section is required to be accompanied with such amount of fee and payable in such manner as may be prescribed. On receipt of a complaint, the District Forum may, by order, allow the complaint to be proceeded with or rejected. However, a complaint shall not be rejected unless an opportunity of being heard has been given to the complainant. It is also to be noted that the admissibility of the complaint shall ordinarily be decided within twenty-one days from the date on which the complaint was received. Where a complaint is allowed to be proceeded, the District Forum may proceed with the complaint in the manner provided under this Act. Where a complaint has been admitted by the District Forum, it shall not be transferred to any other court or tribunal or any authority set up by or under any other law for the time being in force.

The explanation defines the term 'recognised consumer association' as to mean any voluntary consumer association registered under the Companies Act, 1956 or any other law for the time being in force.

Thus, in case the affected consumer is unable to file the complaint due to ignorance, illiteracy or poverty, any recognised consumer association may file the complaint. The rule of 'privity of contract' or locus standi which permits only the aggrieved party to take action has very rightly been set aside in the spirit of public interest

litigation. Section 13 states the procedure to be followed by the District Forum or the State Commission on receipt of a complaint. On receipt of a complaint, a copy of the complaint is to be referred to the opposite party (or each of the opposite parties, where there are more than one) within twenty-one days from the date of its admission, directing him to give his version of the case within a period of 30 days. This period may be extended by another period of 15 days. If the opposite party admits the allegations contained in the complaint, the complaint will be decided on the basis of materials on the record. Where the opposite party denies or disputes the allegations contained in the complaint, or omits or fails to take any action to represent his case within the stipulated time, the dispute will be settled in the following manner:

(i) *In case of dispute relating to any goods*

Where the complaint alleges a defect in the goods which cannot be determined without proper analysis or test of the goods, a sample of the goods shall be obtained from the complainant, sealed and authenticated in the prescribed manner, for referring to the appropriate laboratory for the purpose of any analysis or test whichever may be necessary, so as to find out whether such goods suffer from any such defect. The 'appropriate laboratory' would be required to report its finding to the referring authority, i.e. the District Forum or the State Commission within a period of forty-five days from the receipt of the reference or within such extended period as may be granted by these agencies [Section 13(1)(c)].

The term 'Appropriate laboratory' has been defined to mean a laboratory or organisation recognised by the Central Government or a State Government, subject to such guidelines as may be prescribed by the Central Government in this behalf; or any such laboratory or organisation established by or under any law for the time being in force, which is maintained, financed or aided by the Central Government or a State Government for carrying out analysis or test of any goods with a view to determining whether such goods suffer from any defect.

Section 13 empowers the District Forum/State Commission to require the complainant to deposit such amount as may be specified, towards payment of fees to the 'appropriate laboratory for the purpose of carrying out the necessary analysis or tests. The amount so deposited shall be remitted to the appropriate laboratory to enable it to carry out the analysis and send the report. On receipt of the report, a copy thereof is to be sent by District Forum/State Commission to the opposite party along with its own remarks. In case any of the parties i.e. opposite party or the complainant, disputes the correctness of the methods of analysis/test adopted by the appropriate laboratory, the concerned party will be required to submit his objections in writing in regard to the report.

After giving both the parties a reasonable opportunity of being heard and to present their objections, if any, the District Forum/State Commission shall pass appropriate orders under Section 14 of the Act.

(ii) *In case of dispute relating to goods not requiring testing or analysis or relating to services*

Section 13(2)(b) provides that where the opposite party denies or disputes the allegations contained in the complaint within the time given by the District/State Commission, the Agency concerned shall dispose of the complaint on the basis of evidence tendered by the parties. In case of failure by the opposite party to represent his case within the prescribed time, the complaint shall be disposed of on the basis of evidence tendered by the complainant.

### Limitation Period for Filing of Complaint

Section 24A provides that the District Forum, 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. However, where the complainant satisfies the Forum/Commission as the case may be, that he had sufficient cause for not filing the complaint within two years, such complaint may be entertained by it after recording the reasons for condoning the delay.

### **Administrative Control**

Section 24B authorises the National Commission to exercise administrative control over the State Commissions in the matter of calling for periodical returns regarding the institution, pendency and disposal of cases, issuance of instructions regarding adopting of uniform procedure in hearing of matters, serving copies of documents, translation of judgements etc. and generally overseeing the functioning of the State Commission/District forum to ensure that the objects and purposes of the Act are served in the best possible manner.

Similarly, the State Commission has been authorised to exercise administrative control over all the District forum within its jurisdiction in all the above matters.

### **Powers of the Redressal Agencies**

The District Forum, State Commission and the National Commission have been vested with the powers of a civil court under the Code of Civil Procedure, 1908 while trying a suit in respect of the following matters:

- (i) the summoning and enforcing attendance of any defendant or witness and examining the witness on oath;
- (ii) the discovery and production of any document or other material object producible as evidence;
- (iii) the reception of evidence on affidavits;
- (iv) the requisitioning of the report of the concerned analysis or test from the appropriate laboratory or from any other relevant source;
- (v) issuing of any commission for the examination of any witness; and
- (vi) any other matter which may be prescribed.

Under the Consumer Protection Rules, 1987, the District Forum, the State Commission and the National Commission have the power to require any person:

- (i) to produce before and allow to be examined by an officer of any of these agencies, such books of accounts, documents or commodities as may be required and to keep such book, documents etc. under his custody for the purposes of the Act;
- (ii) to furnish such information which may be required for the purposes of the Act to any officer so specified.

These redressal agencies have also been empowered to pass written orders authorising any officer to exercise the power of entry and search of any premises where the books, papers, commodities or documents are kept if there is any ground to believe that these may be destroyed, mutilated, altered, falsified or secreted. Such authorised officer may also seize books, papers, documents or commodities if they are required for the purposes of the Act, provided the seizure is communicated to the District Forum/State Commission/National Commission within 72 hours. On examination of such documents or commodities, the agency concerned may order the retention thereof or may return it to the party concerned.

The District forum, the State Commission and the National Commission have the power to issue remedial orders to the opposite party directing him to do any one or more of the things referred to in Section 14(1)(a)

to (i) as discussed hereinbelow. The redressal agencies have also been empowered to dismiss frivolous and vexatious complaints under Section 26 of the Act and to order the complainant to make payment of costs, not exceeding Rs. 10,000 to the opposite party.

COMPLAINTS TO BE REGISTERED	
District Consumer Forum	for a claim of Compensation up to Rs.20 lakhs
State Commission	for a claim of Compensation above Rs.20 lakhs and up to Rs.1 crore
National Commission	for a claim of Compensation above Rs.1 crore

### Nature and Scope of Remedies under the Act

*In terms of Section 14(1) of the Act, where the goods complained against suffer from any of the defects specified in the complaint or any of the allegations contained in the complaint about the services are proved, the District Forum/State Commission/National Commission may pass one or more of the following orders:*



- (a) to remove the defects pointed out by the appropriate laboratory from the goods in question;
- (b) to replace the goods with new goods of similar description which shall be free from any defect;
- (c) to return to the complainant the price, or, as the case may be, the charges paid by the complainant;
- (d) to pay such amount as may be awarded by it as compensation to the consumer for any loss or injury suffered by the consumer due to the negligence of the opposite party;
- (e) to remove the defects in goods or deficiencies in the services in question;
- (f) to discontinue the unfair trade practice or the restrictive trade practice or not to repeat them;
- (g) not to offer the hazardous goods for sale;
- (h) to withdraw the hazardous goods from being offered for sale;
- (ha) to cease manufacture of hazardous goods and to desist from offering services which are hazardous in nature;
- (hb) to pay such sum as may be determined by it if it is of the opinion that loss or injury has been suffered by a large number of consumers who are not identifiable conveniently:

It is to be noted that the minimum amount of sum so payable shall not be less than five percent of the value of such defective goods sold or service provided, as the case may be, to such consumers. Further, the amount so obtained shall be credited in favour of such person and utilized in such manner as may be prescribed.

- (hc) to issue corrective advertisement to neutralize the effect of misleading advertisement at the cost of the opposite party responsible for issuing such misleading advertisement;
- (i) to provide for adequate costs to parties.

The remedies that can be granted by the redressal agencies are therefore, wide enough to cover removal of defects/deficiency in goods/services, replacing defective goods with new goods, refunding price/charges paid by the complainant, payment of compensation for loss or damage suffered, providing costs to parties and issuing prohibitory orders directing the discontinuance of unfair trade practice, sale of hazardous goods etc. However, the redressal agencies have not been granted power to order injunctions.

Section 14(1)(d) provides that the redressal agency may order payment of compensation only in the event of negligence of the opposite party which resulted in loss or damage and not otherwise, i.e. even though the complainant has suffered loss or damage, he may not be entitled for compensation if he cannot prove negligence.

### Appeal

Section 15 entitles a person aggrieved by an order of the District Forum to prefer an appeal to the State Commission. Similarly any person aggrieved by any original order of the State Commission may prefer an appeal to the National Commission under Section 19. Likewise, any person aggrieved by any original order of the National Commission may prefer an appeal to the Supreme Court, under Section 23.

All such appeals are to be made within thirty days from the date of the order. However, the concerned Appellate authority may entertain an appeal after the said period of thirty days if it is satisfied that there was sufficient cause for not filling it within the prescribed period. The period of 30 days would be computed from the date of receipt of the order by the appellant.

It may be noted that no appeal by a person, who is required to pay any amount in terms of an order of the District Forum/State Commission, shall be entertained by the State Commission/National Commission respectively unless the appellant has deposited in the prescribed manner fifty percent of that amount or twenty five thousand rupees/thirty-five thousand respectively, whichever is less. It may be observed that appeals are allowable only against the original orders passed by the concerned redressal agency. Appellate orders passed by the State Commission or National Commission (i.e. on appeal against the orders of the District Forum or State Commission) cannot be further appealed against though on questions of law revision petitions may be filed. So also, the revisional orders passed by the State Commission or the National Commission are not appealable.

### APPEL PROVISIONS



*Aggrieved by the orders issued by the District Consumer Redressal Forum, appeal petition may be filed before State Consumer Dispute Redressal Commission within 30 days from the date of receipt of orders.*

*Aggrieved by the orders issued by the State Consumer Dispute Redressal Commission, appeal petition may be filed before National Consumer Dispute Redressal Commission within 30 days from the date of receipt of orders.*

*Aggrieved by the orders issued by the National Consumer Dispute Redressal Commission, appeal petition may be filed before Supreme Court of India within 30 days from the date of receipt of orders*

### Penalties

Section 27 of the Act deals with penalties and provides that failure or omission by a trader or other person against whom a complaint is made or the complainant to comply with any order of the District Forum, State

Commission or the National Commission shall be punishable with imprisonment for a term which shall not be less than one month but which may extend to three years, or with fine of not less than Rs. 2,000 but which may extend to Rs. 10,000, or with both.

However, on being satisfied that the circumstances of any case so require, the District Forum or the State Commission or the National Commission may impose a lesser fine or a shorter term of imprisonment. Section 27(3) prescribes that all offences under the Act to be tried summarily.

### **GIST OF IMPORTANT CONSUMER CASES**

Gist of some of the important rulings rendered by Supreme Court, National Commission and State Commissions, are given hereunder:

#### **Failure to provide basic safeguards in the swimming pool – deficiency in service**

In the case of *Sashikant Krishnaji Dole v. Shitshan Prasarak Mandali* [F.A. No. 134 of 1993 decided on 27.9.1995 (NCDRC)] the school owned a swimming pool and offered swimming facilities to the public on payment of a fee. The school conducted winter and summer training camps to train boys in swimming and for this purpose engaged a trainer/coach. The complainants had enrolled their son for learning swimming under the guidance of the coach. It was alleged that due to the negligence of the coach the boy was drowned and met with his death. The school denied that it had engaged the services of a coach and also denied any responsibility on its part. The coach claimed that he was a person with considerable experience in coaching young boys in swimming and that as in other cases he taught the deceased boy also the way in which he should swim and take all precautions while swimming. When the deceased was found to have been drowned the coach immediately took him out of the water and removed the water from his stomach and gave him artificial respiration and thereafter took him to a doctor, where he died.

The State Commission held the school and the coach deficient in rendering service to the deceased, that the coach was not fully trained, did not exercise even the basic commonsense needed to counter an accident in swimming. He was so casual in his behaviour that he did not attempt to take prompt action to save the life of the deceased and so far as the school was concerned it did not even provide basic facilities nor did it provide any safeguards to prevent accidents.

Dismissing the appeal the National Commission observed that the State Commission had given cogent reasons for holding the school and the coach responsible for death of the deceased. A detailed examination of the depositions of eye witnesses showed that the Commission had correctly appreciated the evidence and come to the conclusion that the coach was negligent and the school did not provide the necessary life saving mechanism to save the lives of trainee students in cases of accidents.

So far as the compensation was concerned the State Commission had taken all relevant factors into account and fixed the amount at Rs. 1.50 lakhs which was reasonable.

#### **Removal of ladder of an aircraft while disembarking by the passenger— deficiency in service**

In *Station Manager, Indian Airlines v. Dr. Jiteswar Ahir* [First Appeal No. 270 of 1994 decided on 28.2.1996 (NCDRC)] when the complainant-passenger occupied his seat in the aircraft, an announcement was made that his luggage was lying on the ground unidentified and that he should disembark to identify his luggage. According to the complainant he moved towards the rear door, and finding that the step ladder was attached to the aircraft door, he stepped out on to the staircase but before he could actually put his entire body weight

on the staircase the ladder was suddenly removed as a result of which he fell down on the ground and sustained bodily injuries which was reported to be about 10 percent. As against the complainant's claim of Rs. 10 lakhs the airlines was willing to pay Rs. 40,000 as compensation which according to them was the maximum statutory liability of the Corporation under the Carriage by Air Act, 1972.

The State Commission, after examining witnesses and the medical boards report held that there was dangerous deficiency in service and having regard to the expert opinion and other medical reports, it ordered payment of compensation of Rs. 4 lakhs and Rs. 1 lakh for mental agony and distress plus costs.

In appeal by the Corporation, the National Commission, upholding the State Commissions order, held that in terms of regulations relied upon by the appellant Corporation, if it was proved that the accident caused to the complainant had resulted in a permanent disablement, incapacitating him from engaging in or being occupied with his usual duties or his business or occupation, the liability could not exceed Rs. 5 lakhs. This case related to the incapacity and permanent disability to the extent of 10 per cent and, therefore, the compensation could not exceed Rs. 5 lakhs. The State Commissions assessment of compensation of Rs. 4 lakhs was justified, considering the age of the complainant (37 years) at the time of accident and his having lost earning capacity. The State Commission was also right in awarding compensation of rupees one lakh for the complainants mental suffering and agony as well as feeling of inferiority in social relations.

Deficiency in service cannot be alleged without attributing fault, imperfection, shortcoming or in adequacy in the quality, nature and manner of performance which is required to be performed by a person in pursuance of a contract or otherwise in relation to any service. The burden of proving deficiency in service is upon the person who alleged it. When the complainant has not established any willful fault, imperfection, shortcoming or inadequacy in the service of the respondent, there can be no deficiency in service.

*In Ravneet Singh Bagga v. KLM Royal Dutch Fintimes [1999(7) SCALE 43]*, the complainant booked a ticket from Delhi to New York by a KLM plane. The airport authorities in New Delhi did not find any fault in his visa and other documents. However at Amsterdam, the airport authorities instituted proceedings of verification because of which the appellant missed his flight to New York. After reaching New York, the airlines tendered apology to the appellant for the inconvenience and paid as a goodwill gesture a sum of Rs. 2,500. The appellant made a complaint to the National Commission under the Consumer Protection Act which was rejected.

The Supreme Court held that the respondent could not be held to be guilty of deficiency in service. The staff of the airline acted fairly and in a bona fide manner, keeping in mind security and safety of passengers and the Aircraft. The photograph on visa documents was a photo copy and not the original which was unusual. In the circumstances, the staff took some time to ascertain the truth and helped the appellant to reach New York the same day.

#### **A doctor qualified to practice homoeopathic system of medicines treating a patient with allopathic medicines and patient dies - guilty of negligence**

*In Poonam Verma v. Ashwin Patel [1996(4) SCALE 364]* the respondent was a qualified medical practitioner in homoeopathic system of medicine. The appellant, was the widow of a person who, it was alleged, had died because of the negligence of the respondent in administering allopathic medicines in which he was not qualified to practise. It was alleged that the deceased was treated to begin with, for viral fever on allopathic medicines and since his condition had not improved antibiotics were used without conducting proper tests. When his condition further deteriorated he was removed to a nursing home and after four days he was removed to a hospital in an unconscious state. Within a few hours thereafter he died.

Her complaint to the National Consumer Disputes Redressal Commission for damages for the negligence

and carelessness of respondent in treating her husband was dismissed. Allowing the appeal the Supreme Court held that the respondent who had practised in allopathy without being qualified in that system was guilty of negligence *per se*. A person is liable at law for the consequences of his negligence.

**Jurisdiction of the Commission:** The Supreme Court observed that it is beyond doubt now that disputes regarding applicability of the Act to persons engaged in medical profession either as private practitioners or as Government doctors working in hospitals or Government dispensaries come within the purview of the Consumer Protection Act, 1986. It is also settled that a patient who is a consumer has to be awarded compensation for loss or injury suffered by him due to negligence of the doctor by applying the same tests as are applied in an action for damages for negligence.

In *Gopi Ram Goyal and others v. National Heart Institute and others*, 2001 CTJ 405 (CP) (NCDRC), the National Commission held that where the record and evidence shows that the conduct of the opposite parties i.e. doctors was more than reasonable and the level of care was as could be expected from professional in exercising reasonable degree of skill and knowledge. The complainant however failed to prove any case of negligence on the part of doctors, therefore the doctor cannot be held liable for death of patient.

#### **Fall from a running train while passing through vestibule passage – deficiency in service**

In *Union of India v. Nathmal Hansaria* [First Appeal No. 692 of 1993 decided on 24.1.1997 (NCDRC)] the daughter of the respondent, travelling by a train, fell down from the running train while she was passing through the inter-connecting passage between two compartments and died as a result of crush injuries on her head. In the respondents petition for compensation, the Railways contended that the Consumer Redressal agencies had no jurisdiction to consider a complaint of this nature in view of Section 15 of the Railway Claims Tribunal Act read with Section 13 of that Act.

The State Commission held that a railway passenger travelling in a train on payment of consideration was a consumer within the meaning of the Consumer Protection Act, 1986. Section 82A of the Railways Act referred to in Section 13 of the Railway Claims Tribunal Act, 1987 and the rules made thereunder provided compensation for railway accidents and not for accidental death of this nature.

Dismissing the appeal the National Commission held that the death of the passenger could not be described as resulting from railway accident but an accidental death caused by the absence of safety devices in the vestibule passage way.

Although the railway administration had claimed that the coach was a new coach and that all coaches had been thoroughly checked at the starting point of the train and that no defect was reported, the railways had not contended that this particular coach was checked at the time of commencement of the journey. The general statement of practice and procedure was not conclusive proof that this particular coach was checked and no evidence had been produced in support of their contention. Thus, the State Commission was right in holding that the deceased passenger was a consumer. On the basis of similar facts, the MRTP Commission has recently awarded a compensation of Rs. 18 lakhs with 9% interest to the parents of deceased. The above compensation appears to be the highest award in commission's history.

#### **Repudiation of Insurance claim because the driver did not have a valid license**

In the case of *Jitendra Kumar v. Oriental Insurance Company Ltd. and another* the Supreme Court has held that where the fire has occurred due to mechanical failure and not due to any act or omission of the driver, the insurance company cannot repudiate the claim because of lack of valid driving license.

**Premium paid to the agent of the LIC but the agent did not deposit the premium, death of the insured - No deficiency of service on the part of the LIC**

*In Harshad J. Shah v. Life Insurance Corporation of India [1997(3) SCALE 423 (SC)]* the insured (since deceased) took out four life policies with double accident benefits, premium payable half-yearly. When the third premium fell due, the general agent of the Corporation met the person and took a bearer cheque towards the premium payable by him in respect of the policies. Although the cheque was encashed immediately thereafter, it was not deposited with the Corporation for another three months. In the meantime, the insured met with a fatal accident and died. The Corporation rejected the widows claim for payment of the sum assured on the ground that the policies had lapsed for non-payment of premium within the grace period.

In the widows complaint to the State Commission under the Consumer Protection Act the Corporation pleaded that the amount of premium allegedly collected by the general agent could not be said to have been received by the Corporation, that the agent was not authorised to collect the premium amount. The State Commission held that in order to collect more business, agents of the Corporation collected premiums from policyholders either in cash or by cheque and then deposited the money so collected with the Corporation and that this practice had been going on directly within the knowledge of the Corporations administration, notwithstanding the departmental instructions that the agent was not authorised to collect the premiums. When the practice of the agent collecting the premiums from policyholders was in existence and the money was collected by the agent in his capacity and authority, the reasonable inference was that the Corporation was negligent in its service towards the policyholder.

The National Commission, in appeal, was of the view that the insurance agent in receiving a bearer cheque from the insured towards payment of insurance premium was not acting as agent of the Corporation nor could it be said that the Corporation had received the premium on the date the bearer cheque was received by the agent, even though he deposited the sum with the Corporation a day after the death of the insured.

Dismissing the appeal the Supreme Court held that the agent had no express authority to receive the premium on behalf of the Corporation. In his letter of appointment there was a condition expressly prohibiting him from collecting the premium. Nor could it be said that he had an implied authority to collect the premium, as regulation 8(4) expressly prohibited the agents from collecting premiums. Therefore, no case had been set up by the complainant before the State Commission that the Corporation by its conduct had induced the policyholders, including the insured, to believe that the agents were authorised to receive premiums on behalf of the Corporation. Nor was there any material on record that lent support to this contention. In the facts of this case there was no room to invoke the doctrine of apparent authority underlying Section 237 of the Indian Contract Act.

*In National Insurance Co. Ltd. v. Seema Malhotra [2001(2) SCALE 140] (Supreme Court)* a cheque was issued under a contract of insurance of motor car by the insured for payment of premium to the policy. However, cheque was dishonoured for want of funds in the account. Meanwhile, the car met an accident and badly damaged, killing the insured owner. The claim for insured amount was repudiated by the company.

The Supreme Court held that applying the principles envisaged under Section 51, 52 and 54 of Indian Contract Act, relating to reciprocal promises, insurer need not to perform his part of promise when the other party fails to perform his part and thus not liable to pay the insured amount.

**Educational Institutions**

*In Sreedharan Nair N. v. Registrar, University of Kerala [2001 CTJ 561 (CP) (NCDRC)]*, the University refused to provide LL.B. degree certificate on completion of course on the ground that the qualifying examination on the basis of which student was admitted in LL.B. course in Kerala law college has not been

recognised by it. The National Commission held that this is a clear case of deficiency on part of University. A compensation of Rs. 50,000 was awarded to complainant.

In *Isabella Thoburn College v. Ms. Fatima Effendi [2001 CTJ 386 (CP) (SCDRC)]*, the State Commission held that non-refund of admission fee is not a deficiency of service on the part of the university because admission fee is consideration for admission and respondent herself voluntarily withdrawing admission from one university to join another institute cannot claim refund of admission fee.

### **Medical Negligence**

In *Kusum Sharma & Others Versus Batra Hospital & Medical Research Centre & Others 2010 CTJ 242 Supreme Court (CP) Supreme Court* held that While deciding whether the medical professional is guilty of medical negligence following well known principles must be kept in view:-

- I.** Negligence is the breach of a duty exercised by omission to do something which a reasonable man, guided by those considerations which ordinarily regulate the conduct of human affairs, would do, or doing something which a prudent and reasonable man would not do.
- II.** Negligence is an essential ingredient of the offence. The negligence to be established by the prosecution must be culpable or gross and not the negligence merely based upon an error of judgment.
- III.** The medical professional is expected to bring a reasonable degree of skill and knowledge and must exercise a reasonable degree of care. Neither the very highest nor a very low degree of care and competence judged in the light of the particular circumstances of each case is what the law requires.
- IV.** A medical practitioner would be liable only where his conduct fell below that of the standards of a reasonably competent practitioner in his field.
- V.** In the realm of diagnosis and treatment there is scope for genuine difference of opinion and one professional doctor is clearly not negligent merely because his conclusion differs from that of other professional doctor.
- VI.** The medical professional is often called upon to adopt a procedure which involves higher element of risk, but which he honestly believes as providing greater chances of success for the patient rather than a procedure involving lesser risk but higher chances of failure. Just because a professional looking to the gravity of illness has taken higher element of risk to redeem the patient out of his/her suffering which did not yield the desired result may not amount to negligence.
- VII.** Negligence cannot be attributed to a doctor so long as he performs his duties with reasonable skill and competence. Merely because the doctor chooses one course of action in preference to the other one available, he would not be liable if the course of action chosen by him was acceptable to the medical profession.
- VIII.** It would not be conducive to the efficiency of the medical profession if no Doctor could administer medicine without a halter round his neck.
- IX.** It is our bounden duty and obligation of the civil society to ensure that the medical professionals are not unnecessary harassed or humiliated so that they can perform their professional duties without fear and apprehension.
- X.** The medical practitioners at times also have to be saved from such a class of complainants who use criminal process as a tool for pressurizing the medical professionals/hospitals particularly private hospitals or clinics for extracting uncalled for compensation. Such malicious proceedings deserve to be discarded against the medical practitioners.

XI. The medical professionals are entitled to get protection so long as they perform their duties with reasonable skill and competence and in the interest of the patients. The interest and welfare of the patients have to be paramount for the medical professionals.

The aforementioned principles must be kept in view while deciding the cases of medical negligence. We should not be understood to have held that doctors can never be prosecuted for medical negligence. As long as the doctors have performed their duties and exercised an ordinary degree of professional skill and competence, they cannot be held guilty of medical negligence. It is imperative that the doctors must be able to perform their professional duties with free mind.

### **LESSON ROUND UP**

- The Consumer Protection Act, 1986 is the most important legislation enacted to provide for better protection of the interests of consumers and for that purpose to make provision for the establishment of consumer councils and other authorities for the settlement of consumer's disputes and for matters connected therewith.
- 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 or promised or partly paid or partly promised, or under any system of deferred payment 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 services 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 beneficiary of such services other than the person who hires or avails of the services for consideration paid or promised, or partly paid and partly promised, or under any system of deferred payment, when such services are availed of with the approval of the first mentioned person but does not include a person who avails of such services for any commercial purpose.
- Defect means any fault, imperfection or shortcoming in the quality, quantity, potency, purity or standard which is required to be maintained by or under any law for the time being in force or under any contract, express or implied, or as is claimed by the trader in any manner whatsoever in relation to any goods.
- Deficiency means any fault, imperfection, shortcoming or inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law for the time being in force or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to any service.
- Commercial purpose does not include use by a consumer of goods bought and used by him exclusively for the purpose of earning his livelihood by means of self-employment.
- A contract for service implies a contract whereby one party undertakes to render services e.g. professional or technical services to or for another in the performance of which he is not subject to detailed direction and control but exercises professional or technical skill and uses his own knowledge and discretion.
- A contract of service on the other hand implies relationship of master and servant and involves an obligation to obey orders in the work to be performed and as to its mode and manner of performance.
- The Act has set up three-tier quasi-judicial consumer disputes redressal machinery at the National, State and District levels, for expeditious and inexpensive settlement of consumer disputes. It also postulates establishment of Consumer Protection Councils at the Central and State levels for the purpose of spreading consumer awareness.
- District Forum has jurisdiction to entertain complaints where the value of goods/services complained against and the compensation, if any claimed, is less than Rs. 20 lakhs, the State Commission for claims exceeding Rs. 20 lakhs but not exceeding Rs. 1 crore; and the National Commission for claims exceeding Rs. 1 crore.
- The District Forum, 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.
- The District Forum, State Commission and the National Commission have been vested with the powers of a civil court under the Code of Civil Procedure, 1908 while trying a suit in respect of the certain matters.

## SELF TEST QUESTIONS

1. Discuss in detail the objects of Consumer Protection Act, 1986.
  2. Briefly discuss the jurisdiction of the various Forums/Commissions under the Consumer Protection Act, 1986?
  3. Explain the nature and scope of the remedies under the Act?
  4. Write short note on the following:
    - (i) Complainant
    - (ii) Deficiency in service
    - (iii) Power of redressal agencies
    - (iv) Consumer.
  5. Discuss consumers rights under Consumer Protection Act, 1986.



# Lesson 4

## INTELLECTUAL PROPERTY RIGHTS

### Section I

#### LESSON OUTLINE

- General Agreement on Tariffs and Trade
- General Agreement on Trade and Services
- World Intellectual Property Organization
- Trade-Related Aspects of Intellectual Property Rights
- Concept and development of Intellectual property Law in India
- Kinds of Intellectual Property
- Meaning of Industrial Property
- Concept of Patents
- Concept of Trade Mark
- Concept of Copyright
- Concept of Geographical Indication
- Concept of Design

#### LEARNING OBJECTIVES

As the term intellectual property relates to the creations of human mind and human intellect, this property is called Intellectual property. Creators can be given the right to prevent others from using their inventions, designs or other creations and to use that right to negotiate payment in return for others using them. These are Intellectual Property Rights.

The creation of Intellectual Property Rights (IPR) is increasingly being recognised in today's global economy and society. Intellectual Property Rights are considered to be the backbone of any economy and their creation and protection is essential for sustained growth of a nation. The intellectual property rights are now not only being used as a tool to protect the creativity and generate revenue but also to build strategic alliances for the socio-economic and technological growth.

The objective of the study is to familiarize the students with the Concept and Development of Intellectual Property Law in India and International Organisation on Intellectual Property Right and International Arrangements dealing with IPR issues.

The areas of intellectual property that it covers are: copyright and related rights (i.e. the rights of performers, producers of sound recordings and broadcasting organizations); trademarks including service marks; geographical indications including appellations of origin; industrial designs; patents including the protection of new varieties of plants; the layout-designs of integrated circuits; and undisclosed information including trade secrets and test data.

## GENERAL AGREEMENT ON TARIFFS AND TRADE (GATT)

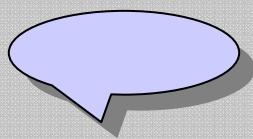
General Agreement on Tariffs and Trade (GATT) contained: (1) an international agreement, i.e. a document setting out the rules for conducting international trade, and (2) an international organization created later to support the agreement. The text of the agreement could be compared to law, the organization was like parliament and the courts combined in a single body. GATT, the international agency, no longer exists. The World Trade Organization has now replaced it. When GATT was created after the Second World War, trade in goods dominated international commerce. Since then, trade in services — transport, travel, banking, insurance, telecommunications, transport, consultancy and so on — has become much more important. So has trade in ideas — inventions and designs, and goods and services incorporating this “intellectual property”. The General Agreement on Tariffs and Trade always dealt with trade in goods, and it still does. It has been amended and incorporated into the new WTO agreements. The updated GATT lives alongside the new General Agreement on Trade in Services (GATS) and Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). The WTO brings the three together within a single organization, a single set of rules and a single system for resolving disputes. In short, the WTO is not a simple extension of GATT. It is much more in existence. While GATT no longer exists as an international organization, the GATT agreement lives on. The old text is now called “GATT 1947”. The updated version is called “GATT 1994”. As the more mature WTO developed out of GATT, one could say that the child is the father of the man.

## GENERAL AGREEMENT ON TRADE IN SERVICES (GATS)

General Agreement on Trade in Services (GATS) is the first ever set of multilateral, legally enforceable rules covering international trade in services. It was negotiated in the Uruguay Round of World Trade Organisation. This was almost half a century after the entry into force of the General Agreement on Tariffs and Trade (GATT) of 1947. Like the agreements on goods, GATS operates on three levels — the main text containing general principles and obligations; annexes dealing with rules for specific sectors; and individual countries' specific commitments to provide access to their markets. Unlike in goods, GATS has a fourth special element lists showing where countries are temporarily not applying the most-favoured-nation principle of non-discrimination.

The GATS' contribution to world services trade rests on two main pillars: (a) ensuring increased transparency and predictability of relevant rules and regulations, and (b) promoting progressive liberalization through successive rounds of negotiations. Within the framework of the Agreement, the latter concept is tantamount to improving market access and extending national treatment to foreign services and service suppliers across an increasing range of sectors. It does not, however, entail deregulation. Rather, the Agreement explicitly recognizes governments' right to regulate, and introduce new regulations, to meet national policy objectives and the particular need of developing countries to exercise this right.

### ***Basic Principles of GATS are as follows:***



- All services are covered by GATS
- Most-favoured-nation treatment applies to all services, except the one-off temporary exemptions
- National treatment applies in the areas where commitments are made
- Transparency in regulations, inquiry points
- Regulations have to be objective and reasonable
- International payments: normally unrestricted
- Individual countries' commitments: negotiated and bound
- Progressive liberalization: through further negotiations

## THE WORLD INTELLECTUAL PROPERTY ORGANIZATION (WIPO)

The World Intellectual Property Organization (WIPO) mission is to promote innovation and creativity for the economic, social and cultural development of all countries, through a balanced and effective international intellectual property system.

The World Intellectual Property Organization (WIPO) is the United Nations agency dedicated to the use of intellectual property as a means of stimulating innovation and creativity. WIPO was established in 1970, following the entry into force of the WIPO Convention in 1967, with a mandate from its Member States to promote the protection of intellectual property throughout the world through cooperation among States and in collaboration with other international organizations. The Organization became a specialized agency of the United Nations in 1974. WIPO headquarters is in Geneva. It dedicated to developing a balanced and accessible international intellectual property (IP) system, which rewards creativity, stimulates innovation and contributes to economic development while safeguarding the public interest. WIPO expanded its role and further demonstrated the importance of intellectual property rights in the management of globalized trade in 1996 by entering into a cooperative agreement with the World Trade Organization.

As part of the United Nations system of specialized agencies, WIPO serves as a forum for its Member States to establish and harmonize rules and practices for the protection of intellectual property rights. WIPO also services global registration systems for trademarks, industrial designs and appellations of origin, and a global filing system for patents. Most industrialized nations have intellectual property protection systems that are centuries old. Many new and developing countries, however, are in the process of building up their patent, trademark and copyright legal frameworks and systems. With the increasing globalization of trade and rapid changes in technological innovation, WIPO plays a key role in helping these new systems to evolve through treaty negotiation, registration, enforcement, legal and technical assistance and training in various forms.

The World Intellectual Property Organization promotes the development and use of the international Intellectual Property system through:

- Services - run systems which make it easier to obtain protection internationally for patents, trademarks, designs and appellations of origin; and to resolve IP disputes.
- Law - develop the international legal IP framework in line with society's evolving needs.
- Infrastructure - build collaborative networks and technical platforms to share knowledge and simplify IP transactions, including free databases and tools for exchanging information.
- Development - build capacity in the use of IP to support economic development.

## TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS (TRIPS)

Ideas and knowledge are an increasingly important part of trade. Most of the value of new medicines and other high technology products lies in the amount of invention, innovation, research, design and testing involved. Films, music recordings, books, computer software and on-line services are bought and sold because of the information and creativity they contain, not usually because of the plastic, metal or paper used to make them. Many products that used to be traded as low-technology goods or commodities now contain a higher proportion of invention and design in their value. For example, brandnamed clothing or new varieties of plants.

Creators can be given the right to prevent others from using their inventions, designs or other creations and to use that right to negotiate payment in return for others using them. These are "intellectual property rights". They take a number of forms. For example books, paintings and films come under copyright; inventions can

be patented; brandnames and product logos can be registered as trademarks; and so on. Governments and parliaments have given creators these rights as an incentive to produce ideas that will benefit society as a whole.

The extent of protection and enforcement of these rights varied widely around the world; and as intellectual property became more important in trade, these differences became a source of tension in international economic relations. New internationally-agreed trade rules for intellectual property rights were seen as a way to introduce more order and predictability, and for disputes to be settled more systematically.

The World Trade Organization's TRIPS Agreement is an attempt to narrow the gaps in the way these rights are protected around the world, and to bring them under common international rules. It establishes minimum levels of protection that each government has to give to the intellectual property of fellow WTO members. In doing so, it strikes a balance between the long term benefits and possible short term costs to society. Society benefits in the long term when intellectual property protection encourages creation and invention, especially when the period of protection expires and the creations and inventions enter the public domain. Governments are allowed to reduce any short term costs through various exceptions.

When there are trade disputes over intellectual property rights, the WTO's dispute settlement system is available. The agreement covers five broad issues:

- how basic principles of the trading system and other international intellectual property agreements should be applied
- how to give adequate protection to intellectual property rights
- how countries should enforce those rights adequately in their own territories
- how to settle disputes on intellectual property between members of the WTO
- special transitional arrangements during the period when the new system is being introduced.

### **Types of intellectual property covered by the TRIPS Agreement**

- Copyright and related rights
- Trademarks, including service marks
- Geographical indications
- Industrial designs
- Patents
- Layout-designs (topographies) of integrated circuits
- Undisclosed information, including trade secret.

### **CONCEPT AND DEVELOPMENT OF INTELLECTUAL PROPERTY LAW IN INDIA**

One of the important feature of the property is that the owner of the property may use his property as he wishes and that no body else can use his property without his authorisation. Of course that right of the proprietor or owner has been limited by the law. Generally, the property can be divided into following three categories:

- (i) Movable property, consisting of movable things;
- (ii) Immovable property, consisting of immovable things, and
- (iii) Intellectual property, consisting of creation of human mind and the human intellect.

## The Concept of Intellectual Property

As the term intellectual property relates to the creations of human mind and human intellect, this property is called Intellectual property. In other words, intellectual property relates to pieces of information which can be incorporated in tangible objects at the same time in an unlimited number of copies at different locations anywhere in the world. The property right does not vest in those copies but in the information reflected in those copies. Similar to property rights in movable and immovable property, intellectual property is also characterised by certain rights as well as limitations such as right to use and licence and also limited duration in the case of copy right and patents.

## Kinds of Intellectual Property

Usually intellectual property is divided into two branches, namely, industrial property and copyright. The Convention establishing World Intellectual Property Organisation, 1967 provides that the intellectual property shall include rights relating to:

- (i) literary, artistic and scientific works;
- (ii) performances of performing artists, phonograms and broadcasts;
- (iii) inventions in the field of human endeavour;
- (iv) scientific discoveries;
- (v) industrial designs;
- (vi) trademarks, service marks, commercial names and designations;
- (vii) protection against unfair competition; and

all other rights resulting from intellectual activity in the industrial, scientific, literary or artistic fields.

Here, it may be clarified that rights relating to (i) and (ii) above constitute copyright, while (iii), (v) and (vi) constitute industrial property. However, scientific discoveries, as mentioned under (iv) above, belongs to neither of two branches of intellectual property, as scientific discoveries and inventions are not the same.

## Meaning of Industrial Property

The expression 'Industrial Property' is sometimes misunderstood as relating to movable or immovable property used for industrial production. However, industrial property is a kind of intellectual property and relates to creation of human mind, e.g., inventions and industrial designs. Simply stated, inventions are new solutions to technological problems, and industrial designs are aesthetic creations determining the appearance of industrial products. In addition, industrial property includes trademarks, service marks, commercial names and designations, including indications of source and appellations of origin, and the protection against unfair competition.

The term 'Industrial Property' may not appear entirely logical in the sense that the inventions are only concerned with the industry. In other words, the inventions are exploited in industrial plants while the trademarks, service marks, trade names and service names are concerned with both the commerce as well as industry. Notwithstanding the lack of logic, this term has acquired a meaning which clearly covers inventions as well as other marks. The Paris Convention also recognised industrial property to cover patent, trademark, service mark, trade names, utility models, industrial designs, indication of source and appellations of origin and the repression of unfair competition.

Hence, industrial property right is a collective name for rights referring to the commercial or industrial

activities of a person. These activities may include the activities of industrial or commercial interests. They may be called inventions, creations, new products, processes of manufacture, new designs or model and a distinctive mark for goods etc.

### **Concept of Patent**

Generally speaking, Patent is a monopoly grant and it enables the inventor to control the output and within the limits set by demand, the price of the patented products. Underlying economic and commercial justification for the patent system is that it acts as a stimulus to investment in the Industrial innovation. Innovative technology leads to the maintenance of and increase in nations stock of valuable, tradeable and industrial assets.

The grant of first patent can be traced as far back as 500 B.C. It was the city dominated by gourmands, it was perhaps the first to grant what we now-a-days call patent right to promote culinary art. For it conferred exclusive rights of sale to any confectioner who first invented a delicious dish. As the practice was extended to other Greek cities and to other crafts and commodities, it acquired a name 'monopoly', a Greek Portmanteau word from mono (alone) and polein (sale).

Evidences of grant to private individuals by kings and rulers of exclusive property rights to inventors dates back to the 14th Century, but their purpose had varied throughout the history. History shows that in 15th Century Venice there had been systematic use of monopoly privileges for inventors for the encouragement of invention. Utility and novelty of the invention were the important considerations for granting a patent privilege. The inventors were also required to put his invention in commercial use within a specified period. In 16th Century the German princes awarded inventors of new arts and machines and also took into consideration the utility and novelty of inventions. Early laws in American colonies served primarily to encourage foreign manufacturers to establish new industries in the colonies by providing them protected domestic markets.

By the late 15th Century, the English monarchy increasingly started using monopoly privilege to reward court favourites, to secure loyalty and to secure control over the industry but these privileges were not used to encourage inventions. In 1623, the English Parliament adopted a Statute of monopolies which recognised the inventors patent as a justifiable monopoly to be distinguished from other monopoly privileges. The Statute outlawed the awarding of monopoly privileges except for first and true inventor of a new manufacture.

In England, during the 16th and 17th Century the inventors patent of monopoly had become of great national importance. From the mid-seventeenth Century through the mid-nineteenth Century, the laws recognising the patent monopoly spread throughout Europe and North America, but these privileges were not granted without the opposition. In India, the law relating to Patents is contained in the Patents Act, 1970, has been amended in the year 1995, 1999, 2002 and 2005 to meet India's obligations under the agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs) forming part of the Agreement establishing the World Trade Organisation (WTO). The Patents Act has been amended keeping in view the development of technological capability in India, coupled with the need for integrating the intellectual property system with international practices and intellectual property regimes. The amendments have also been aimed at making the Act a modern, harmonised and user-friendly legislation to adequately protect national and public interests while simultaneously meeting India's international obligations.

### **Concept of Trade Mark**

A Trade Mark distinguishes the goods of one manufacturer or trader from similar goods of others and therefore, it seeks to protect the interest of the consumer as well as the trader. A trade mark may consist of a

device depicting the picture of animals, human beings etc., words, letters, numerals, signatures or any combination thereof. Since a trade mark indicates relationship in the course of trade, between trader and goods, it serves as a useful medium of advertisement for the goods and their quality. The object of trademark law is to permit an enterprise by registering its trademark to obtain an exclusive right to use, share, or assign a mark. Closely related to trademarks are service marks which distinguish the services of an enterprise from the services of other enterprise.

Trademarks are not a creation of our times, even though their current nature and omnipresence is of rather recent origin. Trademark, a word created only in the 19th century continued to play a significant role in the trade and commerce throughout the major part of history, including medieval times and the centuries beyond. The guilds, one of the mainstays of economies in earlier times, often even required their members, the masters of the various crafts, to affix marks on their products in order to exercise control over their production. The trademarks began to assume their present day role in the course of the eighteenth century with the advent of mass production and growing trade in goods with the establishment of more complicated system of distribution of goods from the producer to the buyer. In the course of time, remedies were developed by the Courts, or the legislations to stop the infringement of trademark rights. One of the first countries to enact a comprehensive law on trademarks, was France in 1857, a law which remained in force for more than 100 years. United Kingdom enacted its Trademarks Registration Act, 1875 providing for the registration of trademarks. Subsequently, various amendments were introduced in the Act of 1857 and finally the Trade Marks Act, 1938 was enacted. As far as the recognition of modern ways of exploiting trademark is concerned, the Trade Marks Act, 1938, since its inception, recognised the assignment of trademarks without the simultaneous transfer of the respective business. The national developments were influenced to a substantial degree by developments in international field, particularly Paris Convention for the Protection of Industrial Property, 1883, including trademarks which is supplement by the Madrid Agreement on Registration of trademarks; signed in 1891. In India, the law relating to Trademarks is contained in the Trade and Merchandise Marks Act, 1958, which has now been replaced by the Trade Mark Act, 1999.

In view of developments in trading and commercial practices, increasing globalisation of trade and industry, the need to encourage investment flows and transfer of technology, need for simplification and harmonization of trade mark management systems and to give effect to important judicial decisions, a new Trade Marks Act, 1999 have been enacted to provide for registration of trade mark for goods as well as services including prohibition to the registration of imitation of well known trade marks, and expansion of grounds for refusal of registration. The Act also simplified the procedure for registration of registered user, enlarged the scope of permitted use and allowed the registration of Collective Marks owned by associations, etc.

The Act also provides for establishment of an Appellate Board for speedy disposal of appeals and rectification applications. The Act empowers the Registrar to register certification trade marks. So far this power was vested with the Central Government. Provision for enhanced punishment for the offences relating to trade marks on the lines of Copyright Act, 1957; restriction on sale of spurious goods; and use of some one elses trade marks as part of corporate names, or name of business concern have also been made in the Act. The new Act amended the definition of trade marks, provides for filing a single application for registration in more than one class and extension of period of registration and renewal from 7 to 10 years. Making trade mark offences cognizable; enlarging the jurisdiction of courts on the lines of Copyright Act; and amplifying the powers of the court to grant ex parte injunction in certain cases, are other notable features of the new Act.

### Concept of Copyright

The idea of Copyright protection only began to emerge with the invention of printing, which made it for literary works to be duplicated by mechanical processes instead of being copied by hand. This led to the

grant of privileges, by authorities and kings, entitling beneficiaries exclusive rights of reproduction and distribution, for limited period, with remedies in the form of fines, seizure, confiscation of infringing copies and possibly damages.

However, the criticism of the system of privileges led to the adoption of the Statute of Anne in 1709, the first copyright Statute. In the 18th century there was dispute over the relationship between copyright subsisting in common law and copyright under the Statute of Anne. This was finally settled by House of Lords in 1774 which ruled that at common law the author had the sole right of printing and publishing his book, but that once a book was published the rights in it were exclusively regulated by the Statute. This common law right in unpublished works lasted until the Copyright Act, 1911, which abolished the Statute of Anne.

Copyright is a well recognised form of property right which had its roots in the common law system and subsequently came to be governed by the national laws in each country. Copyright as the name suggests arose as an exclusive right of the author to copy the literature produced by him and stop others from doing so. There are well-known instances of legal intervention to punish a person for copying literary or aesthetic out put of another even before the concept of copyright took shape. The concept of idea was originally concerned with the field of literature and arts. In view of technological advancements in recent times, copyright protection has been expanded considerably. Today, copyright law has extended protection not only to literary, dramatic, musical and artistic works but also sound recordings, films, broadcasts, cable programmes and typographical arrangements of publications. Computer programs have also been brought within the purview of copyright law.

Thus, the copyright deals with the rights of intellectual creators in their creation. The copyright law deals with the particular forms of creativity, concerned primarily with mass communication. It is also concerned with virtually all forms and methods of public communication, not only printed publications but also with such matters as sound, and television broadcasting, films for public exhibition etc. and even computerised systems for the storage and retrieval of information. The copyright law, however, protects only the form of expression of ideas themselves. The creativity protected by copyright law is creativity in the choice and arrangement of words, musical notes, colours, shapes and so on. In India, the law relating to copyright is governed by the Copyright Act, 1957 which has been amended in 1983, 1984, 1985, 1991, 1992, 1994, 1999 and 2012. The amendment introduced in 1984 included computer program within the definition of literary work and a new definition of computer program was inserted by the 1994 amendment. The philosophical justification for including computer programs under literary work has been that computer programs are also products of intellectual skill like any other literary work.

In 1999, the Copyright Act, 1957 has been amended to give effect to the provisions of Article 14 of the TRIPs agreement providing term of protection to performers rights at least until the end of a period of fifty years computed from the end of the calendar year in which the performance took place. The Amendment Act also inserted new Section 40A empowering the Central Government to extend the provisions of the Copyright Act to broadcasts and performances made in other countries subject to the condition however that such countries extend similar protection to broadcasts and performances made in India. Another new Section 42A empowers the Central Government to restrict rights of foreign broadcasting organisations and performers.

### **Concept of Design**

Industrial designs belong to the aesthetic field, but are at the same time intended to serve as pattern for the manufacture of products of industry or handicraft. An industrial design is the ornamental or aesthetic aspect of a useful article, which must appeal to the sense of sight and may consist of the shape and/or pattern and/or colour of article. An industrial design to be protectable, must be new and original. Industrial designs are protected against unauthorised copying or limitation, for a period which usually lasts for five, ten or 15 years.

Textile designs were the first to receive legal protection. As early as 1787 the first Act for design protection was enacted in Great Britain for the Encouragement of the Arts of design and printing Linens, cotton, calicoes and Muslins, by vesting properties thereof in the Designers, Printers and Proprietors for a limited time. This was an experimental measure extending protection for a limited duration. Shortly thereafter its life was extended and soon afterwards it was made perpetual. In 1839 the protection under the Act was enlarged to cover "Designs for Printing other woven Fabrics".

In the same year another Act was passed for design protection for articles of manufacture generally: An Act to secure to Proprietors of Designs for Articles of Manufacture the Copyright of such Designs for a limited time. The legislative process for design protection took rapid strides thereafter. A consolidating and updating measure enacted in 1842. An Act to consolidate and amend the laws relating to the Copyright of Designs for ornamenting Articles of manufacture-repealed all the earlier statutes referred to above.

It is significant to observe that when the designs law was codified in 1842 and took its modern day shape, copyright protection had not yet been extended to drawings, paintings and photographs. This came only twenty years later with the enactment of the Fine Arts Copyright Act, 1862. Codification of copyright law was nowhere in sight and came only seventy years later with the enactment of the Imperial Copyright Act, 1911. Until 1883 the statutes relating to patents, designs and trade marks remained separate. They were combined in a single enactment by the Patents, Designs, and Trade Marks Act, 1883, which repealed all the then existing statutes in the three areas. Soon trade marks law parted company and was separately enacted as the Trade Marks Act, 1905, leaving patents and designs to remain together. The Patents and Designs Act, 1907, consolidated the enactments relating to patents and designs.

The first designs legislation enacted in India was the Patterns and Designs Protection Act, 1872. It was enacted as a supplement to the Statute-Act 15 of 1859-passed by the Governor-General of India in Council which for the first time made provision for granting to inventors of "new manufacture the exclusive privilege of making, selling and using the invention in India or authorising others to do so for a specified term. The Act of 1872 was passed to extend similar privileges to the inventors of new patterns and designs in British India, though for a very shorter duration of years. It included in the term new manufacture any new and original pattern or design, or the application of such pattern or design to any substance or article of manufacture". The Act, however, left undefined the expression new pattern or design.

The Inventions and Designs Act, 1898, which consolidated and amended the law relating to the protection of inventions and designs contained provisions relating to designs in a separate part. The (British) Patents and Designs Act, 1907, became the basis of the Indian Patents and Designs Act, 1911. The patents provisions of the Indian Patents and Designs Act, 1911, were repealed by the Patents Act, 1970, a post-Independence updating and consolidation of the patents law. The design provisions of the Indian Patents and Designs Act, 1911, continue, with some consequential amendments, with the title as the Designs Act, 1911. The new Designs Act, 2000 has been passed by the Parliament.

### Geographical Indications

Geographical Indications of Goods are that aspect of industrial property which refers to a country or to a place situated therein as being the country or place of origin of that product. Typically, such a name conveys an assurance of quality and distinctiveness which is essentially attributable to the fact of its origin in that defined geographical locality, region or country.

Geographical Indications covered under Articles 22 to 24 of the WTO Trade Related Aspects of Intellectual Property Rights (TRIPS) Agreement, which was part of the Agreements concluding the Uruguay Round of GATT negotiations. India, as a member of the World Trade Organization (WTO), enacted the Geographical

Indications of Goods (Registration & Protection) Act, 1999. In December 1999 and it has come into force with effect from 15th September 2003. This Act seeks to provide for the registration and better protection of geographical indications relating to goods in India. Examples of Indian Geographical Indications are Darjeeling Tea, Kanchipuram Silk Saree, Alphanso Mango, Nagpur Orange, Kolhapuri Chappal etc.,.

### **Amendments to the IP legislations after India became a member of the WTO**

Intellectual Property Right is a private right recognized within the territory of a country and assigned to an individual or individuals for a specific period of time in return for making public, the results of their creativity or innovation.

The Intellectual Property regime of the Government of India underwent significant changes after India's accession to TRIPS in 1995. India became a member of the World Trade Organization in 1995, and this brought about the next round of revisions in the Indian IP system. As per the transitional arrangement it was required to comply with the provisions of TRIPS within a period of 5 years except for the provision relating to extension of product patents to technologies that were hitherto exempt, for which an additional period of 5 years was given. This implied that all IP legislations were required to be compliant with the TRIPS Agreement by the year 2000 with the exception of the Patent legislation which had to be amenable to TRIPS by 2005. To achieve this, the Patents Act, 1970 was modified in a calibrated manner in 1999, 2002 and 2005. The first major amendment to the Patents Act 1970 was made in 1999 (brought into force retrospectively from 1st January, 1995) which allowed for filing of applications for product patents in the areas of drugs, pharmaceuticals and agro-chemicals. The amendment provided for such applications to be examined only after December 2004 and granted exclusive marketing rights to the applicants till then, subject to certain conditions. The second and third major amendments were brought in 2002 and 2005, which included provisions relating to term of patent, incorporation of the provisions on parallel imports and extension of product patents to all technologies including pharmaceutical, agro chemicals etc.

The Trade Marks Act, 1999 was enacted incorporating the developments in trading and commercial practices and the TRIPS provisions. Some of the important amendments in compliance with the TRIPS provisions were the introduction of trade marks for Services and inclusion of the concept of well-known trade mark. The amendment also provided for setting up of the Intellectual Property Appellate Board (IPAB) for hearing appeals against the decision of the Registrar. After the Patent Amendment of 2002, appeals against the decision of the Controller also came to lie before the IPAB instead of the High Courts. In keeping with India's commitment under TRIPS, a new legislation on Geographical Indications namely the Geographical Indication of Goods (Registration and Protection), Act, 1999 was enacted. Further as mandated by TRIPS, Member Countries were required to provide protection to plant varieties either by patents or by an effective *sui generis* system or by any combination thereof. India having ratified the Agreement on Trade Related Aspects of Intellectual Property Rights was obliged to make provision for giving effect to Article 27.3(b) relating to Protection of Plant Varieties. Considering this obligation and national requirement, the Protection of Plant Varieties and Farmers' Rights Act was enacted in 2001.

The Designs Act 1911 was repealed and a new legislation was enacted in the year 2000 with a view to provide more effective protection to registered designs and to promote design activity in the country. New law the Semiconductor Integrated Circuits Layout Design Act 2000 and the Protection of Plant Varieties and Farmers Rights Act 2001 enacted and the Copyright Act, 1957 was amended. These developments paved the way for the intellectual property system as it exists today, mirroring some of the key best practices from across the globe. Today, India's IP system ensures protection of intellectual property while promoting balance of rights and obligations.

## LESSON ROUND UP

- General Agreement on Tariffs and Trade (GATT) contained: (1) an international agreement, i.e. a document setting out the rules for conducting international trade, and (2) an international organization created later to support the agreement.
- General Agreement on Trade in Services (GATS) is the first ever set of multilateral, legally enforceable rules covering international trade in services. It was negotiated in the Uruguay Round of World Trade Organisation.
- The World Trade Organization's TRIPS Agreement is an attempt to narrow the gaps in the way these rights are protected around the world, and to bring them under common international rules. It establishes minimum levels of protection that each government has to give to the intellectual property of fellow WTO members. In doing so, it strikes a balance between the long term benefits and possible short term costs to society.
- The World Intellectual Property Organization (WIPO) mission is to promote innovation and creativity for the economic, social and cultural development of all countries, through a balanced and effective international intellectual property system.
- Intellectual property relates to the creations of human mind and human intellect, this property is called Intellectual property. In other words, intellectual property relates to pieces of information which can be incorporated in tangible objects at the same time in an unlimited number of copies at different locations anywhere in the world. The property right does not vest in those copies but in the information reflected in those copies.

## SELF TEST QUESTIONS

1. Discuss briefly on Intellectual Property Rights.
2. Distinguish between GATT and GATS.
3. Enumerate the concept and development of intellectual property law in India.
4. Discuss the basic principles of GATS.
5. Write short notes on
  - (i) WIPO
  - (ii) TRIPS Agreement.

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# INTELLECTUAL PROPERTY RIGHTS (THE PATENTS ACT, 1970)

## Section II

### LESSON OUTLINE

- Introduction
- Definitions
- Form of Application
- Provisional and complete specification
- Content of specification
- Publication of specification
- Request for Examination
- Examination of Application
- Infringement of patent
- Opposition to the patent
- Term of patent
- Patents of addition
- Restoration of lapsed patents
- Surrender and revocation of patents
- Revocation of patent by controller
- Compulsory licences
- Termination of compulsory license
- International Arrangements
- Patent Agent

### LEARNING OBJECTIVES

Patent is a monopoly grant and it enables the inventor to control the output and within the limits set by demand, the price of the patented products. Underlying economic and commercial justification for the patent system is that it acts as a stimulus to investment in the Industrial innovation. Innovative technology leads to the maintenance of and increase in nations stock of valuable, tradable and industrial assets.

The law relating to patents contained in the Patents Act, 1970 has been amended in the year 1995, 1999, 2002 and 2005 to meet India's obligations under the agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs) forming part of the Agreement establishing the World Trade Organisation (WTO). The Patents Act has been amended keeping in view the development of technological capability in India, coupled with the need for integrating the intellectual property system with international practices and intellectual property regimes.

This section covers legal aspects of Patents and how the Patents Act is a modern, harmonised and user-friendly legislation to adequately protect national and public interests while simultaneously meeting India's international obligations.

“Patent” means a patent for any invention granted under the Patents Act, 1970. “Invention” means a new product or process involving an inventive step and capable for industrial application.

## INTRODUCTION

A Patent is a statutory right for an invention granted for a limited period of time to the patentee by the Government, in exchange of full disclosure of his invention for excluding others, from making, using, selling, importing the patented product or process for producing that product for those purposes without his consent.

The law relating to patents contained in the Patents Act, 1970 .The Patents Act was enacted by the Government of India in the year 1970 in pursuance of its powers under Entry 49 of the List I of Schedule VII of the Constitution of India. List I contains the list of the items in the Union List and Entry 49 reads, "Patents, inventions and designs; copyright; trade-marks and merchandise marks." The Act was notified on 19th September 1970. It has been amended in the year 1995, 1999, 2002 and 2005.

## Definitions

Section 2 of the Patents Act, 1970 defines various terms used in the Act. The definition of some notable terms is given below:

### **Assignee**

Section 2(1) (a) of the Act defines the term assignee as to include the legal representative of a deceased assignee, and references to the assignee of any person include references to the assignee of the legal representative or assignee of that person.

### **Budapest Treaty**

Budapest Treaty has been defined under Section 2(1) (aba) to mean the Budapest Treaty on the International Recognition of the Deposit of Micro-organisms for the Purposes of Patent Procedure done at Budapest on April 28, 1977 as amended and modified from time to time.

### **Convention Application**

Section 2(1) (c) defines the convention application as to mean an application for a patent made by virtue of Section 135.

### **Exclusive Licence**

According to Section 2(1) (f) exclusive licence means a licence from a patentee which confers on the licensee, or on the licensee and persons authorised by him, to the exclusion of all other persons (including the patentee), any right in respect of the patented invention and exclusive licensee shall be construed accordingly.

### **Invention**

Section 2(1) (j) defines invention as to mean a new product or process involving an inventive step and capable of Industrial application.

### **Inventive Step**

Section 2(1) (ja) defines the term 'inventive step' as to mean a feature of an invention that involves technical advance as compared to the existing knowledge or having economic significance or both that makes the invention not obvious to a person skilled in the art.

### **New Invention**

Section 2(1) (l) defines the term new invention as to mean any invention or technology which has not been anticipated by publication in any document or used in the country or elsewhere in the world before

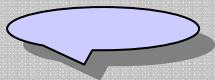
the date of filing of patent application with complete specification, i.e. the subject matter has not fallen into public domain or that it does not form part of the state of the art.

### ***Opposition Board***

The term Opposition Board has been defined under section 2(la) as to mean Opposition Board under section 25(3) of the Act.

### **What are not inventions**

#### ***The following are not inventions within the meaning of Section 3 of the Act:***



- (a) *an invention which is frivolous or which claims anything obviously contrary to well established natural laws;*
- (b) *an invention the primary or intended use or commercial exploitation of which could be contrary to public order or morality or which causes serious prejudice to human, animal or plant life or health or to the environment;*
- (c) *the mere discovery of a scientific principle or the formulation of an abstract theory or discovery of any living thing or non-living substances occurring in nature;*
- (d) *the mere discovery of a new form of a known substance which does not result in the enhancement of the known efficacy of that substance or the mere discovery of any property or mere new use for a known substance or of the mere use of a known process, machine or apparatus unless such known process results in a new product or employs at least one new reactant. Explanation to clause (d) clarifies that salts, esters, polymorphs, metabolites, pure form, particle size, isomers, mixtures of isomers, complexes, combinations and other derivatives of known substance shall be considered to be the same substance, unless they differ significantly in properties with regard to efficacy.*
- (e) *a substance obtained by a mere admixture resulting only in the aggregation of the properties of the components thereof or a process for producing such substance;*
- (f) *the mere arrangement or re-arrangement or duplication of known devices each functioning independently of one another in a known way;*
- (g) *omitted by Patents (Amendment) Act, 2002.*
- (h) *a method of agriculture or horticulture;*
- (i) *any process for the medicinal, surgical, curative, prophylactic diagnostic, therapeutic or other treatment of human beings or any process for a similar treatment of animals to render them free of disease or to increase their economic value or that of their products;*
- (j) *plants and animals in whole or any part thereof other than micro-organisms but including seeds, varieties and species and essentially biological processes for production or propagation of plants and animals;*
- (k) *a computer programme per se other than its technical application to industry or a combination with hardware;*
- (l) *a literary, dramatic, musical or artistic work or any other aesthetic creation whatsoever including cinematographic works and television productions;*
- (m) *a mere scheme or rule or method of performing mental act or method of playing game;*
- (n) *a presentation of information;*
- (o) *topography of integrated circuits;*
- (p) *an invention which in effect, is traditional knowledge or which is an aggregation or duplication of known properties of traditionally known component or components.*

Section 4 prohibits the grant of patent in respect of an invention relating to atomic energy falling within Sub-section (1) of Section 20 of the Atomic Energy Act, 1962.

### **Persons Entitled to make Application for Patent**

Section 6 of the Act provides that an application for a patent for an invention may be made by any of the following persons, that is to say:

- (a) by any person claiming to be the true and first inventor of the invention;
- (b) by any person being the assignee of the person claiming to be the true and first inventor in respect of the right to make such an application;
- (c) by the legal representative of any deceased person who immediately before his death was entitled to make such an application.

The application may be made by one of the persons either alone or jointly with any other person.

### **Form of Application and Provisional & Complete Specification**

Section 7 dealing with form of application requires every application for a patent to be made for one invention only. Where the application is made by virtue of an assignment of the right to apply for a patent for the invention, there shall be furnished with the application proof of the right to make the application.

Every international application under the Patent Cooperation Treaty (PCT) for a patent, as may be filed designating India shall be deemed to be an application under the Act, if a corresponding application has also been filed before Controller in India. The filing date of such application and its complete specification processed by patent office as designated office or elected office shall be the international filing date accorded under the PCT. Section 7(4) provides that every such application, not being a convention application or an application filed under PCT designating India, shall be accompanied by a provisional or a complete specification.

Section 9 stipulates that where an application for a patent (not being a convention application or an application filed under PCT designating India) is accompanied by a provisional specification, a complete specification shall be filed within twelve months from the date of filing of the application, and if the complete specification is not so filed, the application shall be deemed to be abandoned. Where two or more applications in the name of the same applicant are accompanied by provisional specifications in respect of inventions which are cognate or of which one is a modification of another and the Controller is of opinion that the whole of such inventions are such as to constitute a single invention and may properly be included in one patent, he may allow one complete specification to be filed in respect of all such provisional specifications.

However, the period of twelve months shall be reckoned from the date of filing of the earliest provisional specification.

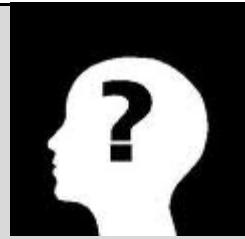
Where an application for a patent (not being a convention application or an application filed under PCT designating India) is accompanied by a specification purporting to be a complete specification, the Controller may, if the applicant so requests at any time within twelve months from the date of filing of the application, direct that such specification shall be treated as a provisional specification and proceed with the application accordingly.

Where a complete specification has been filed in pursuance of an application for a patent accompanied by a provisional specification or by a specification treated by virtue of a direction under sub-section (3) as a provisional specification, the Controller may, if the applicant so requests at any time before the grant of

patent, cancel the provisional specification and post-date the application to the date of filing of the complete specification.

### **Does a Patent obtained in India give protection worldwide?**

*Patent protection is territorial right and therefore it is effective only within the territory of India. However, filing an application in India enables the applicant to file a corresponding application for same invention in convention countries, within or before expiry of twelve months from the filing date in India. Therefore, separate patents should be obtained in each country where the applicant requires protection of his invention in those countries. There is no patent valid worldwide.*



### **Is it possible to file international application under Patent Cooperation Treaty (PCT) in India?**

*It is possible to file an international application known as PCT application in India in the Patent Offices located at Kolkata, Chennai, Mumbai and Delhi. All these offices act as Receiving Office (RO) for International application.*



### **Contents of Specifications**

Section 10 dealing with contents of Specifications provides that every specification, whether provisional or complete, shall describe the invention and begin with a title sufficiently indicating the subject matter to which the invention relates.

Every complete specification is required to -

- (a) fully and particularly describe the invention and its operation or use and the method by which it is to be performed;
- (b) disclose the best method of performing the invention which is known to the applicant and for which he is entitled to claim protection;
- (c) end with a claim or claims defining the scope of the invention for which protection is claimed; and
- (d) be accompanied by an abstract to provide technical information on the invention.

However, the Controller may amend the abstract for providing better information to third parties and if the applicant mentions a biological material in the specification which may not be described in such a way as to satisfy clauses (a) and (b) above and if such material is not available to the public, the application shall be completed by depositing the material to an International Depository Authority under the Budapest Treaty and by fulfilling the following conditions, namely:

- (i) the deposit of the material shall be made not later than the date of filing the patent application in India and a reference thereof shall be made in the specification within the prescribed period;
- (ii) all the available characteristics of the material required for it to be correctly identified or indicated are included in the specification including the name, address of the depository institution and the date and number of the deposit of the material at the institution;

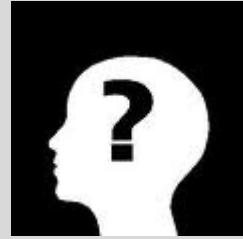
- (iii) access to the material is available in the depository institution only after the date of the application for patent in India or if a priority is claimed after the date of the priority;
- (iv) disclose the source and geographical origin of the biological material in the specification, when used in an invention.

In case of an international application designating India the title, description, drawings, abstracts and claims filed with the application shall be taken as the complete specification for the purposes of the Act.

The claim or claims of a complete specification shall relate to a single invention, or to a group of inventions linked so as to form a single inventive concept, shall be clear and succinct and shall be fairly based on the matter disclosed in the specification.

### ***How a Patent Specification is prepared?***

*A patent specification can be prepared by the applicant himself or his registered and authorized agent. The patent specification generally comprises of the title of the invention indicating its technical field, prior art, draw backs in the prior art, the solution provided by the inventor to obviate the drawbacks of the prior art, a concise but sufficient description of the invention and its usefulness, drawings (if Any) and details of best method of its working. The complete specification must contain at least one claim or statement of claims defining the scope of the invention for which protection is sought for.*



### **Publication of Applications**

Section 11A(1) provides that save as provided otherwise, no application for patents shall ordinarily be open to public for such period as may be prescribed. Sub-section (2) entitles an applicant to request the Controller, in the prescribed manner, to publish his application at any time before the expiry of the period prescribed under sub-section (1) and subject to the provisions of sub-section (3). The Controller on receipt of such request shall publish such application as soon as possible. Every application for patent shall be published on expiry of the period specified in sub-section (1) except those applications in which secrecy direction is imposed under section 35; or application has been abandoned under section 9(1); or application has been withdrawn three months prior to the period specified under sub-section (1).

The publication of every application shall include the particulars of the date of application, number of application, name and address of the applicant identifying the application and an abstract. Upon publication of an application for a patent, the depository institution shall make the biological material mentioned in the specification available to the public. The patent office may, on payment of prescribed fee make the specification and drawings, if any, of such application available to the public.

Section 11A(7) provides that on or from the date of publication of the application for patent and until the date of grant of a patent in respect of such application, the applicant shall have the like privileges and rights as if a patent for invention had been granted on the date of publication of application. However, the applicant shall have no right to institute any proceedings for infringement until the patent has been granted. Additionally, the rights of a patentee in respect of applications made under Section 5(2) before January 1, 2005 shall accrue from the date of grant of patent.

Moreover, after the patent is granted in respect of applications made under Section 5(2), the patent holder shall only be entitled to receive reasonable royalty from such enterprises which have made significant investment and were producing and marketing concerned product prior to January 1, 2005 and which

continue to manufacture the product covered by the patent on the date of grant of the patent and no infringement proceedings shall be instituted against such enterprises.

### **Request for Examination**

Section 11B provides that no application for a patent shall be examined unless the applicant or any other interested person makes a request in the prescribed manner for such examination within the prescribed period. In case of an application in respect of a claim for a patent filed under Section 5(2) before January 1, 2005, a request for examination shall be made in the prescribed manner for such examination within the prescribed period, by the applicant or any other interested person.

In case the applicant or any other interested person does not make a request for examination of the application for a patent within the specified period, the application shall be treated as withdrawn by the applicant. However the applicant may, at any time after filing the application but before the grant of the patent, withdraw the application by making a request in the prescribed manner; and in a case secrecy direction has been issued under Section 35, the request for examination may be made within the prescribed period from the date of revocation of the secrecy direction.

### **Examination of Application**

Section 12 dealing with examination of application provides that when the request for examination has been filed in respect of an application for a patent in the prescribed manner under Section 11B(1) or (3), the application and specification and other documents related thereto shall be referred at the earliest by the Controller to an examiner for making a report to him in respect of the following matters, namely:

- (a) whether the application and the specification and other documents relating thereto are in accordance with the requirements of the Act and of any rules made thereunder;
- (b) whether there is any lawful ground of objection to the grant of the patent in pursuance of the application;
- (c) the result of investigations made under Section 13, and
- (d) any other matter which may be prescribed.

The examiner to whom the application and the specification and other documents relating thereto are referred shall ordinarily make the report to the Controller within the prescribed period.

### **Search for Anticipation by Previous Publication and by Prior Claim**

Section 13 dealing with search for anticipation by previous publication and by prior claim provides that the examiner to whom the application for a patent is referred shall make investigation for the purpose of ascertaining whether the invention so far as claimed in any claim of the complete specification:

- (a) has been anticipated by publication before the date of filing of the applicant's complete specification in any specification filed in pursuance of an application for a patent made in India and dated on or after the 1st day of January, 1912;
- (b) is claimed in any claim of any other complete specification published on or after the date of filing of the applicant's complete specification, being a specification filed in pursuance of an application for a patent made in India and dated before or claiming the priority date earlier than that date.

The examiner shall, in addition, make such investigation for the purpose of ascertaining whether the invention so far as claimed in any claim of the complete specification has been anticipated by publication in India or elsewhere in any document other than those mentioned in Section 13(1) before the date of filing of

the applicant's complete specification. In case a complete specification has been amended before the grant of a patent, the amended specification shall be examined and investigated in the like manner as the original specification.

### **Consideration of the Report of Examiner by Controller**

Section 14 provides that in case the report of the examiner is adverse to the applicant and requires any amendment of the application, specification or other documents, the Controller shall, before proceeding to dispose of the application, communicate the gist of obligations to the applicant as expeditiously as possible and afford him an opportunity of hearing.

### **Power of Controller to Refuse or Require Amended Application in Certain matters**

Section 15 empowers the Controller to refuse the application or to require the application, specification or other documents to be amended, if he is satisfied that the application or any specification or any other document filed in pursuance thereof does not comply with the provisions of the Act and the rules made thereunder.

### **Power of Controller to make Orders Respecting Dating of Application and Cases of Anticipation**

Section 17 provides that at any time after the filing of an application and before the grant of the patent, the Controller may at the request of the applicant direct that the application shall be post-dated to such date as may be specified in the request and proceed with the application accordingly. However, no application shall be post-dated to a date later than six months from the date on which it was actually made or would be deemed to have been made.

Where an application or specification (including drawings) or any other document is required to be amended under Section 15, the application or specification or other document shall, if the Controller so directs, be deemed to have been made on the date on which the requirement is complied with or where the application or specification or other document is returned to the applicant, the date on which it is refiled after complying with the requirement.

Section 18 says that where it appears to the Controller that the invention so far as claimed in any claim of the complete specification has been anticipated, he may refuse the application unless the applicant:

- (a) shows to the satisfaction of the Controller that the priority date of the claim of his complete specification is not later than the date on which the relevant document was published; or
- (b) amends his complete specification to the satisfaction of the Controller.

If it appears to the Controller that the invention is claimed in a claim of any other complete specification, he may, direct that a reference to that other specification be inserted in the applicant's complete specification unless the applicant shows to the satisfaction of the Controller that the priority date of his claim is not later than the priority date of the claim of the said other specification; or the complete specification has been amended to his satisfaction.

Similar provision also applies in the case where it appears to the Controller that the invention so far claimed in any claim of the applicant's complete specification has been claimed in other complete specification referred to in section 13(1)(a) and that such other complete specification was published on or before the priority date of the applicant's claim.

### Potential infringement

Section 19 provides that if in consequence of the investigations it appears to the Controller that an invention in respect of which an application for a patent has been made cannot be performed without substantial risk of infringement of a claim of any other patent, he may direct that a reference to that other patent, be inserted in the applicant's complete specification by way of notice to the public within such time as may be prescribed, unless

- (a) the applicant shows to the satisfaction of the Controller that there are reasonable grounds for contesting the validity of the said claim of the other patent; or
- (b) the complete specification is amended to the satisfaction of the Controller.

The reference shall be inserted in the following form, namely:

"Reference has been directed, in pursuance of Section 19(2) of the Patents Act, 1970 to Patent No. ....".

Where after a reference to another patent has been inserted in a complete specification in pursuance of a direction under Section 19(1):

- (a) that other patent is revoked or otherwise ceases to be in force; or
- (b) the specification of that other patent is amended by the deletion of the relevant claim; or
- (c) it is found, in proceedings before the court or the Controller, that the relevant claim of that other patent is invalid or is not infringed by any working of the applicant's invention, the Controller may, on the application of the applicant delete the reference to that other patent.

### Substitution of applicants etc.

Section 20 says that if the Controller is satisfied, on a claim made in prescribed manner at any time before a patent has been granted that by virtue of any assignment or agreement in writing made by the applicant or one of the applicants for the patent or by operation of law, the claimant would, if the patent were then granted, be entitled thereto or to the interest of the applicant therein, or to an undivided share of the patent or of that interest, the Controller may direct that the application shall proceed in the name of the claimant or in the names of the claimants and the applicant or the other joint applicant or applicants, accordingly as the case may be. No such direction shall however, be given by virtue of any assignment or agreement made by one of the two or more joint applicants for a patent except with the consent of the other joint applicant or applicants. Further, no such direction shall be given by virtue of any assignment or agreement for the assignment of the benefit of an invention unless:

- (a) the invention is identified therein by reference to the number of the applications for the patent; or
- (b) there is produced to the Controller an acknowledgement by the person by whom the assignment or agreement was made that the assignment or agreement relates to the invention in respect of which that application is made; or
- (c) the rights of the claimant in respect of the invention have been finally established by the decision of court; or
- (d) the Controller gives directions for enabling the application to proceed or for regulating the manner in which it should be proceeded with under sub-section (5).

Where one of the two or more joint applicants for a patent dies at any time before the patent has been granted, the Controller may upon a request made by the survivor or survivors and with the consent of the legal representative of the deceased direct that the application shall proceed in the name of the survivor or survivors alone.

If any dispute arises between joint applicants for a patent whether or in what manner the application should be proceeded with, the Controller may upon an application made by any of the parties, and after giving to all parties concerned an opportunity of being heard, give such directions as he thinks fit for enabling the application to proceed in the name of one or more of the parties alone or for regulating the manner in which it should be proceeded with.

### Time for Putting Application in Order for Grant

Section 21 of the Act provides that an application for a patent shall be deemed to have been abandoned unless, the applicant has complied within the prescribed period with all the requirements imposed on him by or under the Act, whether in connection with the complete specification or otherwise in relation to the application from the date on which the first statement of objections to the application or complete specification or other documents related thereto is forwarded to the applicant by the Controller.

Explanation to section 21(1) clarifies that where the application for a patent or any specification or, in the case of a convention application or an application filed under the PCT designating India any document filed as part of the application has been returned to the applicant by the Controller in the course of the proceedings, the applicant shall not be deemed to have complied with such requirements unless and until he has re-filed it or the applicant proves to the satisfaction of the Controller that for the reasons beyond his control such document could not be re-filed.

Sub-section (2) of Section 21 provides that if at the expiration of the period as prescribed under sub-section (1) an appeal to the High Court is pending in respect of the application for the patent for the main invention; or in the case of an application for a patent of addition, an appeal to the High Court is pending in respect of either that application or the application for the main invention, the time within which the requirements of the Controller shall be complied with shall, on an application made by the applicant before the expiration of the period as prescribed under sub-section (1), be extended until such date as the High Court may determine. In case, the time within which the appeal mentioned in sub-section (2) may be instituted has not expired, the Controller may extend the period as prescribed under sub-section (1), to such further period as he may determine. However, in case of an appeal filed during the said further period, and the High Court has granted any extension of time for complying with the requirements of the Controller, then the requirements may be complied with within the time granted by the High Court.

### OPPOSITION TO THE PATENT

Section 25 of the Act deals with opposition to grant of patent and provides that where an application for a patent has been published but a patent has not been granted, any person may, in writing, represent by way of opposition to the Controller against the grant of patent on the following grounds and the Controller on request of such person shall hear him and dispose of the representation in the prescribed manner and specified time:

- (a) that the applicant for the patent or the person under or through whom he claims, wrongfully obtained the invention or any part thereof from him or from a person under or through whom he claims;
- (b) that the invention so far as claimed in any claim of the complete specification has been published before the priority date of the claim —
  - (i) in any specification filed in pursuance of an application for a patent made in India on or after the 1st day of January, 1912; or
  - (ii) in India or elsewhere, in any other document :

Provided that the ground specified in sub-clause (ii) shall not be available where such publication does not constitute an anticipation of the invention by virtue of sub-section (2) or sub-section (3) of section 29;

- (c) that the invention so far as claimed in any claim of the complete specification is claimed in a claim of a complete specification published on or after the priority date of the applicant's claim and filed in pursuance of an application for a patent in India, being a claim of which the priority date is earlier than that of the applicant's claim;
- (d) that the invention so far as claimed in any claim of the complete specification was publicly known or publicly used in India before the priority date of that claim.

*Explanation* — For the purposes of this clause, an invention relating to a process for which a patent is claimed shall be deemed to have been publicly known or publicly used in India before the priority date of the claim if a product made by that process had already been imported into India before that date except where such importation has been for the purpose of reasonable trial or experiment only;

- (e) that the invention so far as claimed in any claim of the complete specification is obvious and clearly does not involve any inventive step, having regard to the matter published as mentioned in clause (b) or having regard to what was used in India before the priority date of the applicant's claim;
- (f) that the subject of any claim of the complete specification is not an invention within the meaning of this Act, or is not patentable under this Act;
- (g) that the complete specification does not sufficiently and clearly describe the invention or the method by which it is to be performed;
- (h) that the applicant has failed to disclose to the Controller the information required by section 8 or has furnished the information which in any material particular was false to his knowledge;
- (i) that in the case of convention application, the application was not made within twelve months from the date of the first application for protection for the invention made in a convention country by the applicant or a person from whom he derives title;
- (j) that the complete specification does not disclose or wrongly mention the source of geographical origin of biological material used for the invention;
- (k) that the invention so far as claimed in any claim of the complete specification is anticipated having regard to the knowledge, oral or otherwise, available within any local or indigenous community in India or elsewhere.

Section 25(2) entitles any interested person to give notice of opposition, to the Controller in the prescribed manner at any time after the grant of patent but before the expiry of a period of one year from the date of publication of grant of a patent, on any of the following grounds :-

- (a) that the patentee or the person under or through whom he claims, wrongfully obtained the invention or any part thereof from him or from a person under or through whom he claims;
- (b) that the invention so far as claimed in any claim of the complete specification has been published before the priority date of the claim in any specification filed in pursuance of an application for a patent made in India on or after the 1st day of January, 1912; or in India or elsewhere, in any other document. However, the ground that the invention so far claimed in any claim of complete specification has been published before the priority date of the claim in India or elsewhere in any other document shall not be available where such publication does not constitute an anticipation of the invention by virtue of section 29(2) or (3);
- (c) that the invention so far as claimed in any claim of the complete specification is claimed in a claim of a complete specification published on or after the priority date of the claim of the patentee and filed in pursuance of an application for a patent in India, being a claim of which the priority date is earlier than that of the claim of the patentee;

- (d) that the invention so far as claimed in any claim of the complete specification was publicly known or publicly used in India before the priority date of that claim.

Explanation to clause (d) of Section 25(3) clarifies that an invention relating to a process for which a patent is granted shall be deemed to have been publicly known or publicly used in India before the priority date of the claim if a product made by that process had already been imported into India before that date except where such importation has been for the purpose of reasonable trial or experiment only.

- (e) that the invention so far as claimed in any claim of the complete specification is obvious and clearly does not involve any inventive step, having regard to the matter published as mentioned in clause (b) or having regard to what was used in India before the priority date of the claim;
- (f) that the subject of any claim of the complete specification is not an invention within the meaning of this Act, or is not patentable under this Act;
- (g) that the complete specification does not sufficiently and clearly describe the invention or the method by which it is to be performed;
- (h) that the patentee has failed to disclose to the Controller the information required by section 8 or has furnished the information which in any material particular was false to his knowledge;
- (i) that in the case of a patent granted on convention application, the application for patent was not made within twelve months from the date of the first application for protection for the invention made in a convention country or in India by the patentee or a person from whom he derives title;
- (j) that the complete specification does not disclose or wrongly mentions the source and geographical origin of biological material used for the invention;
- (k) that the invention so far as claimed in any claim of the complete specification was anticipated having regard to the knowledge, oral or otherwise, available within any local or indigenous community in India or elsewhere.

### **Controller to Treat Application as Application of Opponent**

Section 26 of the Act provides that where in any opposition proceeding the Controller finds that the invention, so far as claimed in any claim of the complete specification, was obtained from the opponent in the manner set out in section 25(2)(a) and revokes the patent on that ground, he may, on request by such opponent made in the prescribed manner, direct that the patent shall stand amended in the name of the opponent; or a part of an invention described in the complete specification was so obtained from the opponent, he may pass an order requiring that the specification be amended by the exclusion of that part of the invention.

Where an opponent has, before the date of the order of the Controller requiring the amendment of a complete specification referred to in section 26(1)(b), filed an application for a patent for an invention which included the whole or a part of the invention held to have been obtained from him and such application is pending, the Controller may treat such application and specification in so far as they relate to the invention held to have been obtained from him, as having been filed, for the purposes of the priority dates of claims of the complete specification, on the date on which the corresponding document was or deemed to have been filed by the patentee in the earlier application but for all other purposes the application of the opponent shall be proceeded with as an application for a patent.

### **Constitution of Opposition Board and its proceeding**

Section 25(3) provides that where any such notice of opposition is duly given under sub-section (2), the

Controller shall notify the patentee and constitute a Board by order in writing to be known as the Opposition Board consisting of such officers as he may determine and refer such notice of opposition alongwith the documents to that Board for examination and submission of its recommendation. Every Opposition Board is required to conduct the examination in accordance with the prescribed procedure. Sub-section (4) provides that the Controller shall on receipt of the recommendation of the Opposition Board and after giving the patentee and the opponent an opportunity of being heard, order either to maintain or amend or revoke the patent.

However, the Controller while passing the order shall not take into account any personal document or secret trial or secret use in case the opposition is based on the grounds mentioned under sub-section (2)(d) & (e). In case the Controller issues an order under sub-section (4) that the patent shall be maintained subject to amendment of the specification or any other document, the patent shall stand amended accordingly.

### **Secrecy of Certain Inventions**

Chapter VII of the Act containing Sections 35-40 provides for secrecy of certain inventions. Section 35 deals with secrecy directions relating to inventions relevant for defence purposes. Section 36 provides for periodical review of secrecy directions, Section 37 deals with consequences, Section 38 deals with revocation, Section 39 prohibits residents from applying for patent outside India without the prior permission and Section 40 deals with liabilities.

### **Secrecy Directions for Defence Purposes**

Section 35 provides that where, in respect of an application, it appears to the Controller that the invention is one of a class notified to him by the Central Government as relevant for defence purposes, or, where otherwise the invention appears to him to be so relevant, he may give directions for prohibiting or restricting the publication of information with respect to the invention or the communication of such information to any person or class of persons specified in the directions.

Sub-section (2) requires the Controller to give notice of the application and the directions so issued to the Central Government. The Central Government, upon receipt of such notice, consider whether the publication of the invention would be prejudicial to the defence of India, and if upon such consideration, it appears to it that the publication of the invention would not so prejudice, give notice to the Controller to that effect, who shall thereupon revoke the directions and notify the applicant accordingly. Sub-section (3) provides that where the Central Government is of the opinion that an invention in respect of which the Controller has not given any directions, is relevant for defence purposes, it may at any time before grant of patent notify the Controller to that effect, and thereupon the Controller shall give notice to the Central Government of the directions issued by him.

### **Review of Secrecy directions**

Section 36 deals with the question as to whether an invention in respect of which directions have been given continues to be relevant for defence purposes and empowers the Central Government to reconsider the direction at intervals of six months from the date of issue of such directions or on a request made by the applicant which is found to be reasonable by the Controller.

On such reconsideration if it appears to the Central Government that the publication of the invention would no longer be prejudicial to the defence of India it shall give notice to the Controller accordingly and the Controller shall thereupon revoke the directions given previously. Sub-section (2) requires the result of every re-consideration to be communicated to the applicant within specified time and prescribed manner.

## **RESIDENTS NOT TO APPLY FOR PATENTS OUTSIDE INDIA WITHOUT PRIOR PERMISSION**

Section 39 of the Act provides that no person resident in India shall, except under the authority of a written permit sought in the prescribed manner and granted by or on behalf of the Controller, make or cause to be made any application outside India for the grant of a patent for an invention unless an application for a patent for the same invention has been made in India, not less than six weeks before the application outside India and either no direction has been given under of section 35(1) in relation to the application in India, or all such directions have been revoked.

Sub-section (2) obliges the Controller to dispose of every such application within the prescribed period. However, if the invention is relevant for defence purpose or atomic energy, the Controller shall not grant permit without the prior consent of the Central Government. Sub-section (3) clarifies that the provisions of section 39 shall not apply in relation to an invention for which an application for protection has first been filed in a country outside India by a person resident outside India.

## **GRANT OF PATENTS**

Section 43 dealing with grant of patents provides that where an application for a patent has been found to be in order for grant of the patent and either the application has not been refused by the Controller by virtue of any power vested in him by the Act; or the application has not been found to be in contravention of any of the provisions of the Act, the patent shall be granted as expeditiously as possible to the applicant or, in the case of a joint application, to the applicants jointly, with the seal of the patent office and the date on which the patent is granted shall be entered in the register. The Controller has been put under obligation to publish the fact that the patent has been granted and thereupon the application, specification and other documents related thereto shall be open for public inspection.

### **Grant of patents subject to conditions**

Section 47 dealing with grant of patents subject to conditions provides that the grant of a patent shall be subject to the conditions that:

- (1) any machine, apparatus or other article in respect of which the patent is granted or any article made by using a process in respect of which the patent is granted, may be imported or made by or on behalf of the Government for the purpose merely of its own use;
- (2) any process in respect of which the patent is granted may be used by or on behalf of the Government for the purpose merely of its own use;
- (3) any machine, apparatus or other article in respect of which the patent is granted or any article made by the use of the process in respect of which the patent is granted, may be made or used, and any process in respect of which the patent is granted may be used by any person, for the purpose merely of experiment or research including the imparting of instructions to pupils; and
- (4) in the case of a patent in respect of any medicine or drug, the medicine or drug may be imported by the Government for the purpose merely of its own use or for distribution in any dispensary, hospital or other medical institution maintained by or on behalf of the Government or any other dispensary, hospital or other medical institution which the Central Government may, having regard to the public service that such dispensary, hospital or medical institution renders, specify in this behalf by notification in the Official Gazette.

## TERM OF PATENT



Section 53 provides that the term of every patent granted after the commencement of the Patents (Amendment) Act, 2002 and the term of every patent which has not expired and has not ceased to have effect, on the date of such commencement, shall be twenty years from the date of filing of application for the patent.

Explanation to Section 53(1) clarifies that the term of patent in case of international applications filed under the Paris Convention Treaty (PCT) designating India, shall be twenty years from the international filing date accorded under the Patent Cooperation Treaty.

A patent shall cease to have effect on the expiration of the period prescribed for the payment of any renewal fee, if that fee is not paid within the prescribed period or within such extended period as may be prescribed. Further on cessation of the patent right due to non-payment of renewal fee or on expiry of the term of patent, the subject matter covered by the said patent shall not be entitled to any protection.

## PATENTS OF ADDITION

Section 54, 55 and 56 deals with patents of addition. Section 54 provides that where an application is made for a patent in respect of any improvement in or modification of an invention described or disclosed in the complete specification, namely the main invention and the applicant also applies or has applied for a patent for that invention or is the patentee in respect thereof, the Controller may, if the applicant so requests, grant the patent for the improvement or modification as a patent of addition.

Where an invention being an improvement in or modification of another invention, is the subject of an independent patent and the patentee in respect of that patent is also the patentee in respect of the patent for the main invention, the Controller may, if the patentee so requests, revoke the patent for the improvement or modification and grant to the patentee a patent of addition in respect thereof, bearing the same date of the patent so revoked. However a patent shall not be granted as a patent of addition unless the date of filing of the application is the same as or later than the date of filing of the application in respect of the main invention. A patent of addition shall not be granted before the grant of the patent for the main invention.

Section 55 deals with term of patents of addition and provides that a patent of addition is granted for a term equal to that of the patent for the main invention or so much thereof as has not expired and remains in force during that term or until the previous ceassure of the patent for the main invention and no longer. No renewal fees is payable in respect of a patent of addition, but if any such patent becomes an independent patent the same fees shall thereafter be payable upon the same dates, as if the patent had been originally granted as an independent patent.

Section 56 which deals with validity of patents of addition provides that the grant of a patent of addition shall not be refused and a patent granted as a patent of addition shall not be revoked or invalidated, on the ground only that the invention claimed in the complete specification does not involve any inventive step having regard to any publication or use of the main invention described in the complete specification relating thereto; or any improvement in or modification of the main invention described in the complete specification of a patent of addition to the patent for the main invention or of an application for such a patent of addition, and the validity of a patent of addition shall not be questioned on the ground that the invention ought to have been the subject of an independent patent. In this context, it is clarified that in determining the novelty of the invention claimed in the complete specification filed in pursuance of an application for a patent of addition regard shall be had also to the complete specification in which the main invention is described.

## RESTORATION OF LAPSED PATENTS

Section 60 provides that where a patent has ceased to have effect by reason of failure to pay any renewal fee within the period prescribed under section 53 or within period as may be allowed under section 142(4), the patentee or his legal representative and where the patent was held by two or more persons jointly, then with the leave of the Controller one or more of them without joining the others, may within eighteen months from the date on which the patent ceased to have effect, make an application for the restoration of the patent.

### Procedure for disposal of applications for restoration of lapsed patents

Section 61 provides that if, after hearing the applicant in cases where the applicant so desires or the Controller thinks fit, the Controller is *prima facie* satisfied that the failure to pay the renewal fee was unintentional and that there has been no undue delay in the making of the application, he shall publish the application in the prescribed manner; and within the prescribed period, any person interested may give notice to the Controller of opposition thereto on either or both of the following grounds that —

- (a) the failure to pay the renewal fee was not unintentional; or
- (b) there has been undue delay in the making of the application.

If notice of opposition is given within the prescribed period aforesaid, the Controller shall notify the applicant, and shall give to him and to the opponent an opportunity to be heard before deciding the case. If no notice of opposition is given within the prescribed period aforesaid or if in the case of opposition, the decision of the Controller is in favour of the applicant, the Controller shall, upon payment of any unpaid renewal fee and such additional fee as may be prescribed, restore the patent and any patent of addition specified in the application which has ceased to have effect on the cesser of that patent. The Controller may, if he thinks fit as a condition of restoring the patent, require that an entry shall be made in the register of any document or matter which has to be entered in the register but which has not been so entered.

### Rights of patentees of lapsed patents which have been restored

Section 62 provides that where a patent is restored, the rights of the patentee shall be subject to such conditions as may be prescribed and to such other conditions as the Controller thinks fit to impose for the protection or compensation of persons who may have begun to avail themselves of, or have taken definite steps by contract or otherwise to avail themselves of, the patented invention between the date when the patent ceased to have effect and the date of the publication of the application for restoration of the patent. No suit or other proceeding shall be commenced or prosecuted in respect of an infringement of a patent committed between the date on which the patent ceased to have effect and the date of the publication of the application for restoration of the patent.

## SURRENDER AND REVOCATION OF PATENTS

Section 63 entitles the patentee to offer to surrender his patent, at any time by giving notice to the Controller. Where such an offer is made, the Controller shall publish the offer in the prescribed manner and also notify every person other than the patentee whose name appears in the register as having an interest in the patent. Any person interested may, within the prescribed period after such publication, give notice of opposition to the Controller and where such notice is given the Controller shall notify the patentee. If the Controller is satisfied after hearing the patentee and any opponent, if desirous of being heard, that the patent may properly be surrendered, he may accept the offer and by order revoke the patent.

Section 64 deals with revocation of patents, section 65 deals with revocation of patent and amendment of complete specification on directions of the Government in cases relating to atomic energy and section 66

deals with revocation of patents in public interest. Section 65 as amended by Patents (Amendment) Act, 2005 provides that where at any time after grant of a patent, the Central Government is satisfied that a patent is for an invention relating to atomic energy for which no patent can be granted under sub-section (1) of section 20 of the Atomic Energy Act, 1962, it may direct the Controller to revoke the patent, and thereupon the Controller, after giving notice, to the patentee and every other person whose name has been entered in the register as having an interest in the patent, and after giving them an opportunity of being heard, may revoke the patent. Sub-section 2 empowers the Controller to allow the patentee to amend the complete specification in such manner as he considers necessary instead of revoking the patent.

### WORKING OF PATENTED INVENTIONS – GENERAL PRINCIPLES

Section 83 dealing with general principles applicable to working of patented invention provides that in exercising the powers conferred for working of patents and compulsory licences, regard shall be had to the following general considerations, namely:

- (a) that patents are granted to encourage inventions and to secure that the inventions are worked in India on a commercial scale and to the fullest extent that is reasonably practicable without undue delay;
- (b) that they are not granted merely to enable patentees to enjoy a monopoly for the importation of the patented article;
- (c) that the protection and enforcement of patent rights contribute to the promotion of technological innovation and to the transfer and dissemination of technology, to the mutual advantage of producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to a balance of rights and obligations;
- (d) that patents granted do not impede protection of public health and nutrition and should act as instrument to promote public interest specially in sectors of vital importance for socio-economic and technological development of India;
- (e) that patents granted do not in any way prohibit Central Government in taking measures to protect public health;
- (f) that the patent right is not abused by the patentee or person deriving title or interest on patent from the patentee, and the patentee or a person deriving title or interest on patent from the patentee does not resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology; and
- (g) that patents are granted to make the benefit of the patented invention available at reasonably affordable prices to the public.

### COMPULSORY LICENCES

Section 84 provides that at any time after the expiration of three years from the date of the grant of a patent, any person interested may make an application to the Controller for grant of compulsory licence on patent on any of the following grounds, namely:

- (a) that the reasonable requirements of the public with respect to the patented invention have not been satisfied, or
- (b) that the patented invention is not available to the public at a reasonably affordable price, or
- (c) that the patented invention is not worked in the territory of India.

An application for compulsory licence may be made by any person notwithstanding that he is already the holder of a licence under the patent and no person shall be estopped from alleging that the reasonable requirements of the public with respect to the patented invention are not satisfied or that the patented invention is not worked in the territory of India or that the patented invention is not available to the public at a reasonably affordable price by reason of any admission made by him, whether in such a licence or otherwise or by reason of his having accepted such a licence.

Sub-section (3) requires every application for compulsory licence to contain a statement setting out the nature of the applicant's interest together with such particulars as may be prescribed and the facts upon which the application is based. The Controller on being satisfied that the reasonable requirements of the public with respect to the patented invention have not been satisfied or the patented invention is not worked in the territory of India or the patented invention is not available to the public at a reasonably affordable price, may grant a licence upon such terms as he may deem fit.

In considering the application of compulsory licence, the Controller is required to take into account —

- (i) the nature of the invention, the time which has elapsed since the sealing of the patent and the measures already taken by the patentee or any licensee to make full use of the invention;
- (ii) the ability of the applicant to work the invention to the public advantage;
- (iii) the capacity of the applicant to undertake the risk in providing capital and working the invention, if the application were granted;
- (iv) as to whether the applicant has made efforts to obtain a licence from the patentee on reasonable terms and conditions and such efforts have not been successful within a reasonable period as the Controller may deem fit.

However, the Controller is under no obligation to take into account matters subsequent to the making of the application. It has been clarified that the reasonable period shall be construed as a period not ordinarily exceeding a period of six months. In this context, it has been clarified that, the reasonable requirements of the public shall be deemed not to have been satisfied if —

- (a) by reason of the refusal of the patentee to grant a licence or licences on reasonable terms,-
  - (i) an existing trade or industry or the development thereof or the establishment of any new trade or industry in India or the trade or industry in India or the trade or industry of any person or class of persons trading or manufacturing in India is prejudiced; or
  - (ii) the demand for the patented article has not been met to an adequate extent or on reasonable terms; or
  - (iii) a market for export of the patented article manufactured in India is not being supplied or developed; or
  - (iv) the establishment or development of commercial activities in India is prejudiced; or
- (b) by reason of conditions imposed by the patentee upon the grant of licences under the patent or upon the purchase, hire or use of the patented article or process, the manufacture, use or sale of materials not protected by the patent, or the establishment or development of any trade or industry in India, is prejudiced; or
- (c) the patentee imposes a condition upon the grant of licences under the patent to provide exclusive grant back, prevention to challenges to the validity of patent or coercive package licensing; or
- (d) the patented invention is not being worked in the territory of India on a commercial scale to an adequate extent or is not being so worked to the fullest extent that is reasonably practicable; or

- (e) the working of the patented invention in the territory of India on a commercial scale is being prevented or hindered by the importation from abroad of the patented article by —
- the patentee or persons claiming under him; or
  - persons directly or indirectly purchasing from him; or
  - other persons against whom the patentee is not taking or has not taken proceedings for infringement.

### REVOCATION OF PATENTS BY THE CONTROLLER FOR NON-WORKING

Section 85 deals with revocation of patents by Controller for non-working and provides that where, in respect of a patent, a compulsory licence has been granted, the Central Government or any person interested may, after the expiration of two years from the date of the order granting the first compulsory licence, apply to the Controller for an order revoking the patent on the ground that the patented invention has not been worked in the territory of India or reasonable requirements of the public with respect to the patented invention has not been satisfied or the patented invention is not available to the public at a reasonably affordable price.

Every application for revocation should contain prescribed particulars, the facts upon which the application is based, and, in the case of an application other than by the Central Government, should also set out the nature of the applicant's interest. The Controller, if satisfied that the reasonable requirements of the public with respect to the patented invention has not been satisfied or patented invention has not been worked in the territory of India or is not available to the public at a reasonably affordable price, may make an order revoking the patent. The controller has however been put under obligation to ordinarily decide such application within one year of its presentation.

### Procedure for dealing with applications

Section 87 provides that where the Controller is satisfied, upon consideration of an application for compulsory licence or revocation of patent, that a *prima facie* case has been made out for the making of an order, he shall direct the applicant to serve copies of the application upon the patentee and any other person appearing from the register to be interested in the patent in respect of which the application is made, and shall publish the application in the Official Journal.

The patentee or any other person desiring to oppose the application may, within prescribed time or within such further time as the Controller may on application allow, give to the Controller notice of opposition. Any such notice of opposition should contain a statement setting out the grounds on which the application is opposed. Where any such notice of opposition is duly given, the Controller shall notify the applicant, and shall give to the applicant and the opponent an opportunity to be heard before deciding the case.

### Powers of Controller in granting compulsory licences

Section 88 provides that where the Controller is satisfied that the manufacture, use or sale of materials not protected by the patent is prejudiced by reason of conditions imposed by the patentee upon the grant of licences under the patent, or upon the purchase, hire or use of the patented article or process, he may order the grant of licences under the patent to such customers of the applicant as he thinks fit as well as to the applicant.

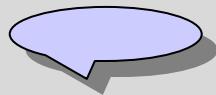
Where an application for compulsory licence is made under Section 84 by a person being the holder of a licence under the patent, the Controller may, if he makes an order for the grant of a licence to the applicant, order the existing licence to be cancelled, or may, if he thinks fit, instead of making an order for the grant of a licence to the applicant, order the existing licence to be amended.

Where two or more patents are held by the same patentee and an applicant for a compulsory licence establishes that the reasonable requirements of the public have not been satisfied with respect to only some of the said patents, then, if the Controller is satisfied that the applicant cannot efficiently or satisfactorily work the licence granted to him under those patents without infringing the other patents held by the patentee and if those patents involve important technical advancement or considerable economic significance in relation to the other patents, he may, by order, direct the grant of a licence in respect of the other patents also to enable the licensee to work the patent or patents in regard to which a licence is granted.

Where the terms and conditions of a licence have been settled by the Controller, the licensee may, at any time after he has worked the invention on a commercial scale for a period of not less than twelve months, make an application to the Controller for the revision of the terms and conditions on the ground that the terms and conditions settled have proved to be more onerous than originally expected and that in consequence thereof the licensee is unable to work the invention except at a loss. However no such application shall be entertained a second time by the Controller.

### Terms and conditions of compulsory licences

***Section 90 provides that in settling the terms and conditions of a compulsory licence, the Controller shall endeavour to secure that —***



- (i) *the royalty and other remuneration, if any, reserved to the patentee or other person beneficially entitled to the patent, is reasonable, having regard to the nature of the invention, the expenditure incurred by the patentee in making the invention or in developing it and obtaining a patent and keeping it in force and other relevant factors;*
- (ii) *the patented invention is worked to the fullest extent by the person to whom the licence is granted and with reasonable profit to him;*
- (iii) *the patented articles are made available to the public at reasonably affordable prices;*
- (iv) *the licence granted is a non-exclusive licence;*
- (v) *the right of the licensee is non-assignable;*
- (vi) *the licence is for the balance term of the patent unless a shorter term is consistent with public interest;*
- (vii) *the licence is granted with a predominant purpose of supply in the Indian market and the licensee may also export the patented product if need be in accordance with section 84(7)(a)(iii).*
- (viii) *in the case of semi-conductor technology, the licence granted is to work the invention for public non-commercial use.*
- (ix) *in case the licence is granted to remedy a practice determined after judicial or administrative process to be anti-competitive, the licensee shall be permitted, if need be, to export the patented product.*

Section 90(2) provides that no licence granted by the Controller shall authorise the licensee to import the patented article or an article or substance made by a patented process from abroad where such importation would, but for such authorisation, constitute an infringement of the rights of the patentee. However in terms of Sub-section (3) the Central Government may direct the Controller to authorise any licensee in respect of a patent to import the patented article or an article or substance made by a patented process from abroad

(subject to such conditions as it considers necessary to impose relating among other matters to the royalty and other remuneration, if any, payable to the patentee, the quantum of import, the sale price of the imported article and the period of importation), if it is necessary to do so in public interest and thereupon the Controller shall give effect to the directions.

### **Licensing of Related Patents**

Section 91 provides that at any time after the sealing of a patent, any person who has the right to work any other patented invention either as patentee or as licensee thereof, exclusive or otherwise, may apply to the Controller for the grant of a licence of the first mentioned patent on the ground that he is prevented or hindered without such licence from working the other invention efficiently or to the best advantage possible. However, no order for grant of such licence shall be made unless the Controller is satisfied that the applicant is able and willing to grant, or procure the grant to the patentee and his licencees if they so desire, of a licence in respect of the other invention on reasonable terms; and the other invention has made a substantial contribution to the establishment or development of commercial or industrial activities in the territory of India.

When the Controller is satisfied that the conditions mentioned in Section 91(1) have been established by the applicant, he may make an order granting a licence under the first mentioned patent and a similar order under the other patent if so requested by the proprietor of the first mentioned patent or his licensee. However the licence granted by the Controller shall be non-assignable except with the assignment of the respective patents.

### **Compulsory licences on Notifications by Central Government**

Section 92 provides that if the Central Government is satisfied, in respect of any patent in force in circumstances of national emergency or in circumstances of extreme urgency or in case of public non-commercial use, that it is necessary that compulsory licences should be granted at any time after the sealing thereof to work the invention, it may make a declaration to that effect, by notification in the Official Gazette, and thereupon the Controller shall on application made at any time, after the notification, by any person interested, grant to the applicant a licence under the patent on such terms and conditions as he thinks fit. In settling the terms and conditions of a licence the Controller shall endeavour to secure that the articles manufactured under the patent shall be available to the public at the lowest prices consistent with the patentees deriving a reasonable advantage from their patent rights.

### **Compulsory Licence for Export of Patented Pharmaceutical Products in Certain Exceptional Circumstances**

Patents (Amendment) Act, 2005 inserted new section 92A dealing with compulsory licence for export of patented pharmaceutical products in certain exceptional circumstances. The new section provides that compulsory licence shall be available for manufacture and export of patented pharmaceutical products to any country having insufficient or no manufacturing capacity in the pharmaceutical sector for the concerned product to address public health problems, provided compulsory licence has been granted by such country or such country has, by notification or otherwise allowed importation of patented pharmaceutical products from India. Sub-section (2) empowers the Controller, on receipt of an application in the prescribed manner, to grant, on such terms and conditions as he may specify, a compulsory licence solely for manufacture and export of the concerned pharmaceutical product to such country.

Explanation to Section 92A defines the pharmaceutical products as to mean any patented product, or product manufactured through a patented process, of the pharmaceutical sector needed to address public health problems and shall be inclusive of ingredients necessary for their manufacture and diagnostic kits required for their use.

## Termination of compulsory licence

Section 94 provides that on an application made by the patentee or any other person deriving title or interest in the patent, a compulsory licence may be terminated by the Controller, provided the circumstances that give rise to the grant thereof no longer exist and such circumstances are unlikely to recur. In this regard the holder of the compulsory licence has been entitled to object to such termination.

## INTERNATIONAL ARRANGEMENTS

Section 133 to 139 deal with international arrangements. Section 133 deals with convention countries; section 134 deals with notification as to countries not providing for reciprocity; section 135 provides for convention applications; section 136 contains special provisions relating to convention applications; section 137 provides for multiple priorities; section 138 deals with supplementary provisions as to convention applications; and section 139 provides for application of other provisions of the Act to convention applications.

In terms of Section 133 a convention country is that country, which is a signatory or party or a group of countries, union of countries or intergovernmental organizations which are signatories or parties to an international, regional or bi-lateral treaty, convention or arrangement to which India is also a signatory or party and which affords to the applicants for patents in India or to citizens of India similar privileges as are granted to their own citizens or citizens to their member countries in respect of the grant of patents and protection of patent rights.

Section 134 provides that where any country notified by the Central Government as Convention Country does not accord to citizens of India the same rights in respect of the grant of patents and the protection of patent rights as it accords to its own nationals, no national of such country shall be entitled either solely or jointly with any other person:

- (a) to apply for the grant of a patent or be registered as the proprietor of a patent;
- (b) to be registered as the assignee of the proprietor of a patent; or
- (c) to apply for a licence or hold any licence under a patent granted under the Act.

Section 135 provides that where a person has made an application for a patent in respect of an invention in a convention country (basic application) and that person or legal representative or assignee of that person makes an application under the Act for a patent within twelve months after the date on which the basic application was made, the priority date of a claim of the complete specification being a claim based on matter disclosed in the basic application, is the date of making of the basic application. The explanation to Section 135(1) clarifies that where applications have been made for similar protection in respect of an invention in two or more convention countries, the period of twelve months shall be reckoned from the date on which the earlier or earliest of the said applications was made. In case of an application filed under the Patent Cooperation Treaty designating India and claiming priority from a previously filed application in India, the provisions of sub-sections (1) and (2) shall apply as if the previously filed application were the basic application. However, a request for examination under section 11B shall be made only for one of the applications filed in India.

Section 136 containing special provisions relating to convention applications requires every convention application to be accompanied by a complete specification; and specify the date on which and the

convention country in which the application for protection, or as the case may be, the first of such application was made; and to state that no application for protection in respect of the invention had been made in a convention country before that date by the applicant or by any person from whom he derives title.

A complete specification filed with a convention application may include claims in respect of developments of, or additions to, the invention in respect of which the application for protection was made in a convention country, being developments or additions in respect of which the applicant would be entitled under the provisions of Section 6 to make a separate application for a patent. Sub-section (3) prohibits a convention application to be post-dated to a date later than the date on which the application could have been made under the Act.

Section 138 requires the applicant of a convention application to furnish, in addition to the complete specification, copies of the specifications or corresponding documents filed or deposited by the applicant in the patent office of the convention country and verified to the satisfaction of the Controller within the prescribed period from the date of communication by the Controller. If any such specification or other document is in a foreign language, a translation into English of the specification or document verified by affidavit or otherwise to the satisfaction of the Controller are required to be furnished.

## PATENT AGENT

The work relating to drafting of specifications, making of application for a patent, subsequent correspondence with the Patent office on the objections raised, representing the applicant's case at the hearings, filing opposition and defending application against opposition is entrusted to a qualified Patent Agent. Sections 125-132 of the Patents Act, 1970 deal with the Patent Agents.

### Qualifications for Registration as Patent Agent

Section 126 provides that a person shall be qualified to have his name entered in the register of patent agent, if he is a citizen of India, completed the age of 21 years, has obtained a degree in science, engineering or technology from any university established under law for the time being in force in the territory of India or possesses such other equivalent qualifications as the Central Government may specify in this behalf and in addition has passed the qualifying examination prescribed for the purpose or has, for a total period of not less than ten years, functioned either as an examiner or discharged the functions of the Controller under Section 73 or both, but cease to hold any such capacity at the time of making the application for registration and paid prescribed fees. However, a person who has been registered as a patent agent before the commencement of Patents (Amendment) Act, 2005 shall be entitled to continue to be, or when required to be re-registered, as a patent agent, on payment of prescribed fee.

Section 132 entitles the applicant for a patent to draft any specification or appear or act before the Controller. Section 132 also allows an advocate, not being a patent agent, to take part in any proceeding before the Controller on behalf of a party who is taking part in any proceeding under the Act.

### Rights and Powers of the Patent Agent

Section 127 empowers the patent agent to practice before the Controller and to prepare all documents, transact all business and discharge such other functions as may be prescribed in connection with any proceeding before the Controller under the Act. In accordance with the provisions of section 128, the patent agent may sign under authorisation in writing in this behalf by the person concerned all applications and communication to the Controller.

## LESSON ROUND UP

- A Patent is a statutory right for an invention granted for a limited period of time to the patentee by the Government, in exchange of full disclosure of his invention for excluding others, from making, using, selling, importing the patented product or process for producing that product for those purposes without his consent.
- The law relating to patents contained in the Patents Act, 1970 has been amended in the year 1995, 1999, 2002 and 2005 to meet India's obligations under the agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs) forming part of the Agreement establishing the World Trade Organisation (WTO).
- Invention as to mean a new product or process involving an inventive step and capable of Industrial application.
- Inventive step as to mean a feature of an invention that involves technical advance as compared to the existing knowledge or having economic significance or both that makes the invention not obvious to a person skilled in the art.
- Provisional specification describes the nature of the invention to have the priority date of filing of the application in which the inventive idea has been disclosed. It must be followed by a complete specification describing the details of the invention along with a statement of claims within 12 months after filing of the provisional application. If the complete specification is not filed within the prescribed period, the application is treated as deemed to have been abandoned.
- Generally, an application filed with provisional specification is known as provisional application which is useful in establishing a priority date for your invention. Moreover, filing of a provisional application is useful as it gives sufficient time to the applicant to assess and evaluate the market potential of his invention before filing complete specification. However, it is not necessary to file an application with provisional specification and one can file application directly with complete specification.
- Application for a patent for an invention may be made (a) by any person claiming to be the true and first inventor of the invention;(b) by any person being the assignee of the person claiming to be the true and first inventor in respect of the right to make such an application;(c)by the legal representative of any deceased person who immediately before his death was entitled to make such an application.
- Patents Act deals with opposition to grant of patent and provides that where an application for a patent has been published but a patent has not been granted, any person may, in writing, represent by way of opposition to the Controller against the grant of patent on the certain grounds.
- The work relating to drafting of specifications, making of application for a patent, subsequent correspondence with the Patent office on the objections raised, representing the applicant's case at the hearings, filing opposition and defending application against opposition is entrusted to a qualified Patent Agent.

## SELF TEST QUESTIONS

1. Discuss in detail the provisions of the Patents Act in relation to compulsory licences.
2. Discuss in detail the provisions relating to patent in addition.
3. Write short note on the following:
  - (i) Inventive step.
  - (ii) Patent agent.
4. Discuss the grounds on which the registration of a patent can be refused?
5. Elaborate the provisions relating to infringement of patent.





# INTELLECTUAL PROPERTY RIGHTS (TRADE MARKS ACT, 1999)

## Section III

### LESSON OUTLINE

- Introduction
- Trade Marks
- Well Known Trade Mark
- Registrar and Trade Mark Registry
- Procedure for and duration of registration of Trade Mark
- Effect of registration
- Assignment and Transmission of Trade Mark
- Infringement of trademark
- Use of trademark
- Registered users
- Rectification and Correction of the register
- Collective marks
- Certification trade marks
- Appellate Board
- Offences, penalties and procedure
- Offences by companies
- Trademark Agent

### LEARNING OBJECTIVES

A Trade Mark distinguishes the goods of one manufacturer or trader from similar goods of others and therefore, it seeks to protect the interest of the consumer as well as the trader. A trade mark may consist of a device depicting the picture of animals, human beings etc., words, letters, numerals, signatures or any combination thereof. Since a trade mark indicates relationship in the course of trade, between trader and goods, it serves as a useful medium of advertisement for the goods and their quality.

The current law of Trade Marks contained in the Trade Marks Act, 1999 is in harmony with two major international treaties on the subject, namely The Paris Convention for Protection of Industrial Property and TRIPS Agreement to both of which India is a signatory.

The Trade Marks Act, 1999 and the Trade Marks Rules, 2002 govern the law relating to Trade Marks in India. Object of trademark law is to permit an enterprise by registering its trademark to obtain an exclusive right to use, share, or assign a mark. Closely related to trademarks are service marks which distinguish the services of an enterprise from the services of other enterprise. Therefore, students should be well versed in The Trade Marks Act, 1999 and Rules made thereunder.

The Trade Marks Act, 1999 is an Act to amend and consolidate the law relating to trade marks, to provide for registration and better protection of trade marks for goods and services and for the prevention of the use of fraudulent marks. It extends to the whole of India.

## INTRODUCTION

A trade mark is a visual symbol which may be a word signature, name, device, label, numerals or combination of colours used by one undertaking on goods or services or other articles of commerce to distinguish it from other similar goods or services originating from a different undertaking.

In view of developments in trading and commercial practices, increasing globalisation of trade and industry, the need to encourage investment flows and transfer of technology, need for simplification and harmonization of trade mark management systems and to give effect to important judicial decisions, a new Trade Marks Act, 1999 have been enacted to provide for registration of trade mark for goods as well as services including prohibition to the registration of imitation of well known trade marks, and expansion of grounds for refusal of registration.

### ***A trade mark performs four functions***



- *It identifies the goods / or services and its origin.*
- *It guarantees its unchanged quality.*
- *It advertises the goods/services.*
- *It creates an image for the goods/ services.*

## Definitions and Interpretations

Following are some of the important terms defined in the Act

### ***“Certification Trade Mark”***

Section 2(1)(e) defines the term certification trade mark as to mean a mark capable of distinguishing the goods or services in connection with which it is used in the course of trade which are certified by the proprietor of the mark in respect of origin, material, mode of manufacture of goods or performance of services, quality, accuracy or other characteristics from goods or services not so certified and registerable as such in respect of those goods or services in the name, as proprietor of the certification trade mark, of that person.

### ***‘Mark’***

The term mark under Section 2(1)(m) has been defined to include a device, brand, heading, label, ticket, name, signature, word, letter, numeral, shape of goods, packaging or combination of colours or any combination thereof.

### ***‘Package’***

In terms of clause (q) of Section 2(1) the term package include any case, box, container, covering, folder, receptacle, vessel, casket, bottle, wrapper, label, band, ticket, reel, frame, capsule, cap, lid, stopper and cork.

**'Permitted Use'**

Section 2(1)(r) defines the term permitted use, in relation to a registered trade mark, as to mean the use of trade mark-

- (i) by a registered user of the trade mark in relation to goods or services -
  - (a) with which he is connected in the course of trade; and
  - (b) in respect of which the trade mark remains registered for the time being; and
  - (c) for which he is registered as registered user; and
  - (d) which complies with any conditions or limitations to which the registration of registered user is subject; or
- (ii) by a person other than the registered proprietor and registered user in relation to goods or services
  - (a) with which he is connected in the course of trade; and
  - (b) in respect of which the trade mark remains registered for the time being; and
  - (c) by consent of such registered proprietor in a written agreement; and
  - (d) which complies with any conditions or limitations to which such user is subject and to which the registration of the trade mark is subject.

**'Service'**

The term service under clause (z) of Sub-section (1) of Section (2) has been defined as to mean service of any description which is made available to potential users and includes the provision of services in connection with business of any industrial or commercial matters such as banking, communication, education, financing, insurance, chit funds, real estate, transport, storage, material treatment, processing, supply of electrical or other energy, boarding, lodging, entertainment, amusement, construction, repair, conveying of news or information and advertising.

**'Trade mark'**

The term trade mark has been defined under Section 2(1)(zb) of the Act as to mean a mark capable of being represented graphically and which is capable of distinguishing the goods or services of one person from those of others and may include shape of goods, their packaging and combination of colours; and

- (i) in relation to Chapter XII (other than section 107), a registered trade mark or a mark used in relation to goods or services for the purpose of indicating or so as to indicate a connection in the course of trade between the goods or services, as the case may be, and some person having the right as proprietor to use the mark; and
- (ii) in relation to other provisions of this Act, a mark used or proposed to be used in relation to goods or services for the purpose of indicating or so to indicate a connection in the course of trade between the goods or services, as the case may be, and some person having the right, either as proprietor or by way of permitted user, to use the mark whether with or without any indication of the identity of that person, and includes a certification trade mark or collective mark.

**'Well-Known Trade Mark'**

In terms of Section 2(1)(zg), a well known trade mark in relation to any goods or services means a mark which has become so to the substantial segment of the public which uses such goods or services such that the use of such mark in relation to other goods or services would be likely to be taken as indicating a

connection in the course of trade or rendering of services between those goods or services and a person using the mark in relation to the first-mentioned goods or services.

### Appointment of Registrar and Trade Mark Registry

Section 3 provides for appointment of the Registrar and other officers and Section 4 empowers the Registrar to withdraw any matter pending before an officer and deal with such matter himself or transfer it to another officer with reasons for such transfer to be recorded therein.

Section 5 deals with the establishment of the Trade Marks Registry and branch offices and provides that the Trade Marks Registry established under the Trade and Merchandise Marks Act, 1958 shall continue to be the Trade Marks Registry for the purposes of this Act.

### Single Register of Trade Marks

Section 6 contains provisions relating to maintenance of a single Register of Trade Marks at Head Office including therein particulars of registered trade marks and other prescribed particulars, except notice of trust. A copy of the Register is to be kept at each branch office. Sub-section (2) allows the maintenance of records in computer floppies or diskettes or in any other electronic form subject to the prescribed safeguards.

### Classification of Goods and Services and Publication of Index

Section 7 empowers the Registrar to classify goods and services according to international classification of goods and services and to determine any question related thereto. Section 8 requires the Registrar to publish an alphabetical index of classification of goods and services.

#### **Prerequisites for a trade mark to be registered**



- *The selected mark should be capable of being represented graphically (that is in the paper form).*
- *It should be capable of distinguishing the goods or services of one undertaking from those of others.*
- *It should be used or proposed to be used mark in relation to goods or services for the purpose of indicating or so as to indicate a connection in the course of trade between the goods or services and some person have the right to use the mark with or without identity of that person.*

### Absolute Grounds for Refusal of Registration

Section 9(1) of the Act containing provisions relating to absolute grounds for refusal for registration prohibit the registration of those trade marks which are devoid of any distinctive character or which consist exclusively of marks or indications which may serve in trade to designate the kind, quality, quantity, intended purpose, etc., or which consist exclusively of marks or indications which have become customary in the current language or in the bona fide and established practices of the trade. However, a trademark shall not be refused registration, if the mark has in fact acquired a distinctive character as a result of use or is a well known trade mark before the date of application. In short, a trade mark which has been demonstrated to be distinctive in the market place shall be regarded as distinctive in law as well and be registerable.

Sub-section (3) prohibits registration of a mark, if it consists exclusively of shape of goods which result from the nature of the goods themselves or which is necessary to obtain a technical result or which gives substantial value to the goods. It is, however, explained that the nature of goods or services in relation to which the Trade Mark is used or proposed to be used shall not be a ground for refusal of registration.

### Relative Grounds for Refusal of Registration

Section 11 stipulates that where there exists a likelihood of confusion on the part of the public because of the identity with an earlier trade mark or similarity of goods or services, the trade mark shall not be registered. The registration of a mark which is merely reproduction or imitation of well-known mark is also prohibited. Accordingly, it has been stipulated that a trade mark which is identical with or similar to an earlier trade mark and is to be registered for good or services which are not similar to those for which the earlier trade mark is registered in the name of a different proprietor, shall not be registered if and to the extent the earlier trade mark is well known trade mark in India and the use of the later trade mark without due cause would take unfair advantage of or be detrimental to the distinctive character or repute of the earlier trade mark. Sub-section (3) prohibits the registration of a trade mark, if or to the extent that, its use will be prevented by law of passing off or under the law of copyright unless the proprietor of earlier trade mark consents to such registration.

The Explanation to this section defines the term Earlier trade mark as to mean a registered trade mark or a convention application which has a date of application earlier than the trade mark in question, or a trade mark, which on the date of application or on the date of priority claimed was entitled to protection as a well known trade mark. Sub-section (5) entitles the proprietor of earlier trade mark, to oppose the registration and prove it. The Act provides that in an opposition proceeding the Registrar shall protect a well-known trade mark against identical or similar trade marks and take into consideration the bad faith of either the applicant or the opponent affecting the rights relating to the trade mark. This section also lays down the factors which the Registrar is required to take into account while determining the status of a well-known trade mark. The Act also lays down the facts to be considered by the Registrar in determining whether a trade mark is known or recognised in a relevant section of the public.

### Procedure for Registration

Section 18 deals with the procedure for making an application for registration. Any person claiming to be the Proprietor of a trademark used or proposed to be used by him, who is desirous of registering it, shall apply in writing to the Registrar in the prescribed manner for the registration of his trademark. Sub-section (2) of Section 18 allows registration in several classes of goods or services by means of a single application. However, the fee payable is to be calculated on the basis of the number of classes in which registration is sought.

Section 23 places obligation on the Registrar to register the trade mark where the procedure for registration of a trade mark has been completed viz., the application has been accepted and either the application has not been opposed or the opposition has been dismissed.

### Duration, Renewal, Removal and Restoration of Registration

Section 25 of the Act deals with duration, renewal of registration, for removal and restoration of registration. It allows registration of a trademark for a period of 10 years. In keeping with the generally accepted international practice and to reduce the work-load of the Trade Marks Office, Section 25 allows renewal of registration for successive periods of 10 years, from the date of the original registration or the last renewal. With a view to facilitate renewal of registration, Section 25(4) provides for restoration of removed trade marks on payment of renewal fee.

### Infringement of Registered Trade Marks

Section 29 dealing with infringement of trade marks, explicitly enumerates the grounds which constitute infringement of a trademark. This section lays down that when a registered trade mark is used by a person

who is not entitled to use such a trade mark under the law, it constitutes infringement. This section clearly states that a registered trade mark is infringed, if

- (a) the mark is identical and is used in respect of similar goods or services; or
- (b) the mark is similar to the registered trade mark and there is an identity or similarity of the goods or services covered by the trade mark; or
- (c) the trade mark is identical and is used in relation to identical goods or services;

and that such use is likely to cause confusion on the part of the public or is likely to be taken to have an association with the registered trade mark. Additionally in respect of cases falling in category (c) above, there will be a legal presumption of likelihood of confusion on the part of the public.

A person shall be deemed to have infringed a registered trade mark, if he uses a mark which is identical with or similar to the registered trade mark, and is used in relation to goods or services which are not similar to those for which trademark is registered; and the registered trade mark has a reputation in India and the use of the mark without due cause would take unfair advantage of or is detrimental to the distinctive character or repute of the registered trade mark. A person has also been prohibited from adopting someone else's trade mark, as his trade name or name of his business concern or part of the name of his business concern dealing with goods or services in respect of which trade mark is registered. A person shall be deemed to have used a registered trade mark in circumstances which include affixing the mark to goods or packaging, offering or exposing the goods for sale or supply of services, importing or exporting the goods, the use of the mark as trade name or trade mark on business paper or in advertising. A person shall be deemed to have infringed a trade mark if he applies such registered trade mark knowing that application of such mark is not authorised by the proprietor or licensee. Advertising of a trade mark to take unfair advantage of, or against the reputation of the trade mark also constitutes an infringement under Section 29(8) of the Act. Where the distinctive element of a registered trade mark consists of words, the spoken use of such words as well as visual representation for promoting the sale of goods or promotion of service would constitute infringement under Sub-section (9) of the Act.

### **Limits on Effect of Registered Trade Mark**

Section 30 enumerates certain acts which do not constitute infringement. This section explicitly states that there will be no infringement, if the use of a mark is in accordance with honest practices in industrial or commercial matters and is not such as to take unfair advantage of or be detrimental to the distinctive character or repute of a trade mark. This section further enumerates the following acts as not constituting an infringement of trade mark:

- (i) where the use is in relation to goods or services to indicate the kind, quality, quantity, etc. of the goods or of rendering of services, or other characteristics of goods or services.
- (ii) where a trade mark is registered subject to conditions or limitations, the use of the trade mark in a manner outside the scope of registration.
- (iii) where a person uses the mark in relation to goods or services for which the registered owner had once applied the mark, and had not subsequently removed it or impliedly consented to its use.
- (iv) a trade mark registered for any goods may be used in relation to parts and accessories to other goods or services and such use is reasonably necessary and its effect is not likely to deceive as to the origin.
- (v) the use of a registered trade mark being one of two or more registered trade marks which are identical or nearly resemble each other, in exercise of the right to the use of that registered trade mark.

### Deceptive Similarity



*In Mahendra and Mahendra Paper Mills Ltd. Vs. Mahindra and Mahindra Ltd. [AIR 2002 SC 117] Supreme Court broadly stated, in an action for passing off on the basis of unregistered trade mark generally for deciding the question of deceptive similarity the following factors are to be considered—*

- *The nature of the marks i.e. whether the marks are word marks or labels marks or composite marks i.e. both words and label works.*
- *The degree of resemblance between the marks, phonetically similar and hence similar in idea.*
- *The nature of the goods in respect of which they are used as trade marks.*
- *The similarity in nature, character and performance of the goods of the rival traders*
- *Class of purchasers who are likely to buy the goods bearing the marks they require, on their education and intelligence and a degree of care they are likely to exercise in purchasing and /or using the goods.*
- *The mode of purchasing the goods or placing orders for the goods.*
- *Any other surrounding circumstances which may be relevant in the extant of dissimilarity between the competing marks.*

Weightage to be given to each of the aforesaid factors depending upon facts of each case and the same weightage cannot be given to each factor in every case.

### Registration to be *prima facie* evidence of validity

Section 31 of the Act stipulates that in all legal proceedings relating to trade mark registered under the Act, the original registration and all subsequent assignments and transmission thereof shall be *prima facie* evidence of its validity. However, as per Section 34 the proprietor or a registered user of a registered trademark is not entitled to interfere with or restrain the use by any person of a trademark identical with or nearly resembling it in relation to goods or services in relation to which that person or a predecessor in title of his has continuously used that trade mark from a prior date.

Therefore, in case of unregistered marks, the owner of the trade mark may lodge a case against passing off action in case his trademark is used by some other person. It has been held by the courts in various cases and the ownership of a trademark is decided by its usage in commercial transactions.

### Inherently Distinctive marks



*The Supreme Court in Uniply Industries Ltd. v. Unicorn Plywood Pvt. Ltd. and Others observed that*

- (i) *for inherently distinctive marks ownership is governed by priority of use for such marks. The first user of sale of goods/services is the owner who is senior to others.*
- (ii) *These marks are given legal protection against infringement immediately upon adoption and use in trade.*
- (iii) *Some courts indicate that even prior sales of goods – though small in size with the mark – are sufficient to establish priority, the test being to determine continuous prior user and the volume of sale or the degree of familiarity of the public with the mark.*

*Therefore, the proprietorship of the trademark is decided by the date of usage of the mark by a person in business transactions.*

### **Assignment and Transmission**

Section 37 entitles the registered proprietor of a trademark to assign the trade mark and to give effectual receipts for any consideration for such assignment. Section 38 deals with the assignability and transmissibility of a registered trade mark with or without goodwill of the business either in respect of all goods or services or part thereof. Section 39 provides that unregistered trade mark may be assigned or transmitted with or without the goodwill of the business concerned.

Section 40 contains restriction on assignments or transmissions of trade mark where multiple exclusive rights would be created in more than one person in relation to same goods or services; same description of goods or services; goods or services or description of goods or services which are associated with each other, which would be likely to deceive or cause confusion. Nevertheless, such assignment is not deemed to be invalid, if having regard to the limitations imposed, the goods are to be sold in different markets - either within India or through exports.

The Act under Section 42 stipulates conditions for assignment of a trade mark without goodwill of business. Such an assignment shall not take effect unless the assignor obtains directions of the Registrar and advertises the assignment in accordance with the directions of the Registrar and as per the prescribed manner.

Section 43 deals with the assignability and transmissibility of certification trade marks and provides that the assignment of certification trade mark can only be done only with the consent of the Registrar. Section 44 states that associated trade marks shall be assignable and transmissible only as a whole but they will be treated as separate trade marks for all other purposes. Section 45 deals with the procedure for registration of assignment and transmission and provides that where the validity of an assignment is in dispute between the parties, the Registrar may refuse to register the assignment or transmission unless the rights of parties are determined by the competent court.

### **Proposed Use of Trade Mark by Company to be formed etc.**

Section 46 empowers the Registrar to allow registration of a trademark, if he is satisfied that (i) a company is about to be formed and registered under the Companies Act and that the applicant intends to assign the trademark to that company with a view to use thereof in relation to those goods and services by the company or (ii) the proprietor intends it to be used by a person, as a registered user after the registration of trademark.

### **Removal of Trade Mark for Non-use**

Section 47 deals with removal of a trade mark from the register on the ground of non-use and provides that a trade mark which is not used within five years of its registration, becomes liable for removal either completely or in respect of those goods or services for which the mark has not been used. The five years period starts from the date on which the trade mark is actually entered on the register. However, Section 47(3) protects a mark from being removed from the register on ground of non-use if such non-use is shown to have been due to special circumstances in the trade which may include restriction imposed by any law or regulation on the use of trade mark in India.

### **Registered User**

Section 48 deals with registered users. Section 49 provides for registration as registered user. Section 50 deals with the power of the Registrar to vary or cancel registration as registered user on the ground that the registered user has used the trade mark otherwise than in accordance with the agreement or in such a way as to cause or likely to cause confusion, or deception or the proprietor/registered user misrepresented or has failed to disclose any material facts for such registration or the stipulation in the agreement regarding the

quality of goods is not enforced or the circumstances have changed since the date of registration, etc. However, Registrar has been put under obligation to give reasonable opportunity of hearing before cancellation of registration.

In view of the simplification of the procedure for registration of registered user and to ascertain whether the registered user agreement is in force, Section 51 empowers the Registrar to require the proprietor to confirm at any time during the continuation of registration as registered user, whether the agreement, on the basis of which registered user was registered is still in force, and if such confirmation is not received within a period of one month, the Registrar shall remove the entry thereof from the Register in the prescribed manner. Section 52 recognises the right of registered user to take proceedings against infringement. Section 54 provides that the registered user will not have a right of assignment or transmission. However, it is clarified that where an individual registered user enters into partnership or remains in a reconstituted firm, the use of the mark by the firm would not amount to assignment or transmission.

### **Collective Marks**



*Collective Marks means a trades mark distinguish the goods or services of members of an association of person not being a partnership within the meaning of the Indian Partnership Act, 1932 which is the proprietor of the mark from those of others.*

Sections 61 to 68 contain provisions relating to the registration of Collective trade marks. These sections provide for registration of a collective mark which belongs to a group or association of persons and the use thereof is reserved for members of the group or association of persons. Collective marks serve to distinguish characteristic features of the products or services offered by those enterprises. It may be owned by an association which may not use the collective mark but whose members may use the same. The association ensures compliance of certain quality standards by its members, who may use the collective mark if they comply with the prescribed requirements concerning its use. The primary function of a collective mark is to indicate a trade connection with the Association or Organisation.

### **Certification Trade Marks**



*Certification trade mark as to mean a mark capable of distinguishing the goods or services in connection with which it is used in the course of trade which are certified by the proprietor of the mark in respect of origin, material, mode of manufacture of goods or performance of services, quality, accuracy or other characteristics from goods or services not so certified and registerable as such in respect of those goods or services in the name, as proprietor of the certification trade mark, of that person.*

Sections 69 to 78 deal with registration of certification trade mark. The purpose of certification trade mark is to show that the goods on which the mark is used have been certified by some competent person in respect of certain characteristics of the goods such as origin, mode of manufacture, quality, etc. The proprietor of a certification trade mark does not himself deal in the goods. A certification trade mark may be used in addition to the users own trade mark on his goods. Central Government empower the final authority for registration of certification trade mark to the Registrar.

### **Intellectual Property Appellate Board**

Sections 83-100 deal with the constitution of an Intellectual Property Appellate Board to hear appeals against the decisions of the Registrar and matters incidental thereto. Section 83 deals with establishment of Appellate Board; Section 84 provides for composition; Section 85 deals with qualifications for appointment as

Chairman, Vice-chairman and members of Appellate Board; Section 86 provides for term of office; Section 88 deals with salaries allowance etc.; Section 89 deals with resignation and removal; Section 90 deals with staff of Appellate Board and Section 91 provides for appeal to Appellate Board.

Section 92 empowers the Appellate Board to prescribe its own procedure. The Appellate Board will have the powers of a Civil Court trying a suit under the Code of Civil Procedure, 1908. With a view to facilitate speedy disposal of cases, this section lays down that the Board shall not be bound by the procedure laid down in the Code of Civil Procedure, 1908 but be guided by the principles of natural justice. Section 93 bars any Court or other authority from exercising jurisdiction, powers or authority in relation to the appeals under Section 91 of the Act.

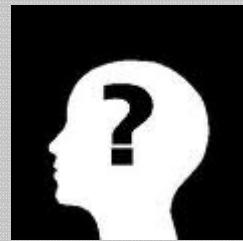
### **Who benefits from a trade mark?**

**Registered Proprietor:** *The Registered Proprietor of a trade mark can stop other traders from unlawfully using his trade mark, sue for damages and secure destruction of infringing goods and or labels.*

**Government:** *The Trade Marks Registry is earning revenue.*

**Professionals:** *The Trade Marks Registration system is driven by professionals like Company Secretaries who act as trademark agents for the clients in the processing of the trade marks application.*

**Purchaser** and ultimately **Consumers** of trade marks goods and services.



### **Offences and Penalties**

Sections 101 to 121 deal with the matters relating to offences, penalties and procedure. Some of the important provisions are discussed below.

#### ***Penalty for Applying False Trade Marks, Trade Descriptions etc.***

Section 103 deals with the penalty for applying false trade mark, trade description, etc.. Accordingly, the penalty for applying false trade mark or false trade description, etc. shall be imprisonment for a term which shall not be less than six months but which may extend to three years and with fine which shall not be less than fifty thousand rupees but which may extend to two lakh rupees. However, the court has been empowered, for adequate and special reasons to be mentioned in the judgement, to impose a sentence lower than the normal punishment.

#### ***Penalty for Falsely Representing a Trademark as Registered***

Section 107 makes it an offence if a person falsely represent a trade mark as registered. Section 107(3) clarifies that the use in relation to a trade mark of the word registered or any other expression, symbol or sign referring whether expressly or impliedly to registration shall be deemed to import a reference to registration in the register, except

- (i) where that word or other expression, symbol or sign is used in direct association with other words delineated in characters at least as large as those in which that word or other expression, symbol or sign is delineated and indicating that the reference is to registration as a trade mark under the law of a country outside India being a country under the law of which the registration referred to is in fact in force; or
- (ii) where that other expression, symbol or sign is of itself such as to indicate that the reference is to such registration as is mentioned above; or

- (iii) where that word is used in relation to a mark registered as a trade mark under the law of a country outside India and in relation solely to goods to be exported to that country or in relation to services for use in that country.

### **Penalty for Improperly Describing a Place of Business as Connected with the Trade Marks Office**

In terms of Section 108, the use of any words which would lead to the belief that a persons place of business is officially connected with the Trade Mark Office shall be treated as offence and punishable with imprisonment for a term which may extend to two years or fine or with both.

Section 109 provides penalty for falsification of entries in the register. The offence is punishable with imprisonment extending upto two years or fine or with both.

### **Offences by Companies**

Section 114 deals with offences by companies and provides that where a person committing offence is a company, every person incharge of and responsible to the company for the conduct of its business will be liable. Where a person accused proves that the offence was committed without his knowledge or he has exercised all due diligence to prevent the commission of such offence, he will not be liable. However, where it is proved that an offence has been committed with the consent or connivance or is attributable to any neglect of any Director, Manager, Secretary or any other officer of the company, he shall be deemed to be guilty of the offence. Explanation to this section defines a company as to mean body corporate and includes a firm or other association of individuals. The explanation also defines director in relation to a firm, as to mean a partner in the firm.

### **Trade Mark Agent**

Section 145 deals with agents and provide that if any act is required to be done before the Registrar by any person, this may be done by a person duly authorised in the prescribed manner who is a legal practitioner, a trade marks agent or by his employee if he is duly authorised by him.

### **LESSON ROUND UP**

- Trade Mark distinguishes the goods of one manufacturer or trader from similar goods of others and therefore, it seeks to protect the interest of the consumer as well as the trader. A trade mark may consist of a device depicting the picture of animals, human beings etc., words, letters, numerals, signatures or any combination thereof.
- The Trade Marks Act, 1999 and the Trade Marks Rules, 2002 govern the law relating to Trade Marks in India.
- Object of trademark law is to permit an enterprise by registering its trademark to obtain an exclusive right to use, share, or assign a mark. Closely related to trademarks are service marks which distinguish the services of an enterprise from the services of other enterprise.
- Mark includes a device, brand, heading, label, ticket, name, signature, word, letter, numeral, shape of goods, packaging or combination of colours or any combination thereof.
- A trade mark performs four functions: It identifies the goods/or services and its origin; It guarantees its unchanged quality; It advertises the goods/services; It creates an image for the goods/ services.
- A well known trade mark in relation to any goods or services means a mark which has become so to the substantial segment of the public which uses such goods or services such that the use of such mark in relation to other goods or services would be likely to be taken as indicating a connection in the course of trade or rendering of services between those goods or services and a person using the mark in relation to the first-mentioned goods or services.

- When a registered trade mark is used by a person who is not entitled to use such a trade mark under the law, it constitutes infringement.
  - A person shall be deemed to have infringed a registered trade mark, if he uses a mark which is identical with or similar to the registered trade mark, and is used in relation to goods or services which are not similar to those for which trademark is registered; and the registered trade mark has a reputation in India and the use of the mark without due cause would take unfair advantage of or is detrimental to the distinctive character or repute of the registered trade mark.
  - There will be no infringement of trade mark, if the use of a mark is in accordance with honest practices in industrial or commercial matters and is not such as to take unfair advantage of or be detrimental to the distinctive character or repute of a trade mark.
  - The registered proprietor of a trademark to assign the trade mark and to give effectual receipts for any consideration for such assignment.
  - A trade mark which is not used within five years of its registration becomes liable for removal either completely or in respect of those goods or services for which the mark has not been used.
  - Intellectual Property Appellate Board to hear appeals against the decisions of the Registrar.

## **SELF TEST QUESTIONS**

1. What is a trade mark?
  2. How to apply for a trade mark in respect of particular goods or services?
  3. Discuss in detail the provisions relating to registered user of trademarks.
  4. Benefit from trademark to all stakeholders. Comment.
  5. Discuss Penal provisions for Falsely Representing a Trademark.

# INTELLECTUAL PROPERTY RIGHTS (COPYRIGHT LAW AND ENFORCEMENT)

## Section IV

### LESSON OUTLINE

- Introduction
- Artistic Work
- Commercial Rental
- Right Management Information
- Meaning of Copyright
- Term of Copyright
- Assignment of Copyright
- Mode of Assignment
- Copyright Board
- Copyright Society
- International Copyright
- Registration of Copyright
- Infringement of Copyright
- Statutory Exception
- Remedies against Infringement of Copyright
- Author Special Right
- Offences and Penalty
- Power of Police to seize Infringement Copies

### LEARNING OBJECTIVES

Copyright deals with the rights of intellectual creators in their creation. The copyright law deals with the particular forms of creativity, concerned primarily with mass communication. It is also concerned with virtually all forms and methods of public communication, not only printed publications but also with such matters as sound, and television broadcasting, films for public exhibition etc. and even computerised systems for the storage and retrieval of information.

The copyright law, however, protects only the form of expression of ideas themselves. The creativity protected by copyright law is creativity in the choice and arrangement of words, musical notes, colours, shapes and so on. In India, the law relating to copyright is contained in Copyright Act 1957, which was last amended in the year 2012.

This section covers legal aspects of copyright protection, their assignments, protection from infringements, moral right of author and statutory exceptions under Copyright Act, 1957. The objective of the study is to familiarize the students with the legal requirements stipulated under the Act.

The Copyright Act, 1957 protects original literary, dramatic, musical and artistic works and cinematograph films and sound recordings from unauthorized uses. Under Article 9.2. of TRIPS Agreements, copyright protects the expressions and not the ideas. There is no copyright protection for ideas, procedures, methods of operation or mathematical concepts as such.

## INTRODUCTION

Copyright is a well recognised form of property right which had its roots in the common law system and subsequently came to be governed by the national laws in each country. Copyright as the name suggests arose as an exclusive right of the author to copy the literature produced by him and stop others from doing so. There are well-known instances of legal intervention to punish a person for copying literary or aesthetic output of another even before the concept of copyright took shape. The concept of idea was originally concerned with the field of literature and arts. In view of technological advancements in recent times, copyright protection has been expanded considerably. Today, copyright law has extended protection not only to literary, dramatic, musical and artistic works but also sound recordings, films, broadcasts, cable programmes and typographical arrangements of publications. Computer programs have also been brought within the purview of copyright law.

In India, the law relating to copyright is governed by the Copyright Act, 1957 which has been amended in 1983, 1984, 1985, 1991, 1992, 1994, 1999 and 2012. The amendment introduced in 1984 included computer program within the definition of literary work and a new definition of computer program was inserted by the 1994 amendment. The philosophical justification for including computer programs under literary work has been that computer programs are also products of intellectual skill like any other literary work.

In 1999, the Copyright Act, 1957 has been amended to give effect to the provisions of Article 14 of the TRIPs agreement providing term of protection to performers rights at least until the end of a period of fifty years computed from the end of the calendar year in which the performance took place. The Amendment Act also inserted new Section 40A empowering the Central Government to extend the provisions of the Copyright Act to broadcasts and performances made in other countries subject to the condition however that such countries extend similar protection to broadcasts and performances made in India. Another new Section 42A empowers the Central Government to restrict rights of foreign broadcasting organisations and performers.

The Act is now amended in 2012 with the object of making certain changes for clarity, to remove operational difficulties and also to address certain newer issues that have emerged in the context of digital technologies and the Internet. Moreover, the main object to amendments the Act is that in the knowledge society in which we live today, it is imperative to encourage creativity for promotion of culture of enterprise and innovation so that creative people realise their potential and it is necessary to keep pace with the challenges for a fast growing knowledge and modern society.

### **Why should copyright be protected?**

*Copyright ensures certain minimum safeguards of the rights of authors over their creations, thereby protecting and rewarding creativity. Creativity being the keystone of progress, no civilized society can afford to ignore the basic requirement of encouraging the same. Economic and social development of a society is dependent on creativity. The protection provided by copyright to the efforts of writers, artists, designers, dramatists, musicians, architects and producers of sound recordings, cinematograph films and computer software, creates an atmosphere conducive to creativity, which induces them to create more and motivates others to create.*



## DEFINITIONS

Section 2 of the Act defines the terms used in the Act. The definition of some notable terms is given below:

**"Adaptation"** means,-

- (i) in relation to a dramatic work, the conversion of the work into a non-dramatic work;
- (ii) in relation to a literary work or an artistic work, the conversion of the work into a dramatic work by way of performance in public or otherwise;
- (iii) in relation to a literary or dramatic work, any abridgement of the work or any version of the work in which the story or action is conveyed wholly or mainly by means of pictures in a form suitable for reproduction in a book, or in a newspaper, magazine or similar periodical;
- (iv) in relation to a musical work, any arrangement or transcription of the work; and
- (v) in relation to any work, any use of such work involving its re-arrangement or alteration;

**"Artistic work"** means-

- (i) a painting, a sculpture, a drawing (including a diagram, map, chart or plan), an engraving or a photograph, whether or not any such work possesses artistic quality;
- (ii) work of architecture; and
- (iii) any other work of artistic craftsmanship;

**"Author"** means,-

- (i) in relation to a literary or dramatic work, the author of the work;
- (ii) in relation to a musical work, the composer;
- (iii) in relation to an artistic work other than a photograph, the artist;
- (iv) in relation to a photograph, the person taking the photograph;
- (v) in relation to a cinematograph or sound recording the producer; and
- (vi) in relation to any literary, dramatic, musical or artistic work which is computer-generated, the person who causes the work to be created

**"Broadcast"** means communication to the public-

- (i) by any means of wireless diffusion, whether in any one or more of the forms of signs, sounds or visual images; or
- (ii) by wire, and includes a re-broadcast;

**"cinematograph film"** means any work of visual recording and includes a sound recording accompanying such visual recording and "cinematograph" shall be construed as including any work produced by any process analogous to cinematography including video films;

**"Commercial rental"** does not include the rental, lease or lending of a lawfully acquired copy of a computer programme, sound recording, visual recording or cinematograph film for non-profit purposes by a non-profit library or non-profit educational institution.

However, a "non-profit library or nonprofit educational institution" means a library or educational institution which receives grants from the Government or exempted from payment of tax under the Income-Tax Act, 1961.

**"Communication to the public"** means making any work or performance available for being seen or heard or otherwise enjoyed by the public directly or by any means of display or diffusion other than by issuing physical copies of it, whether simultaneously or at places and times chosen individually, regardless of whether any member of the public actually sees, hears or otherwise enjoys the work or performance so made available.

However, communication through satellite or cable or any other means of simultaneous communication to more than one household or place of residence including residential rooms of any hotel or hostel shall be deemed to be communication to the public;

**"Composer"**, in relation to a musical work, means the person who composes the music regardless of whether he records it in any form of graphical notation;

**"Computer programme"** means a set of instructions expressed in words, codes, schemes or in any other form, including a machine readable medium, capable of causing a computer to perform a particular task or achieve a particular result;

**"Dramatic work"** includes any piece for recitation, choreographic work or entertainment in dumb show, the scenic arrangement or acting form of which is fixed in writing or otherwise but does not include a cinematograph film;

**"Exclusive licence"** means a licence which confers on the licensee or on the licensee and persons authorised by him, to the exclusion of all other persons (including the owner of the copyright), any right comprised in the copyright in a work, and "exclusive licensee" shall be construed accordingly;

**"Government work"** means a work which is made or published by or under the direction or control of-

- (i) the Government or any department of the Government;
- (ii) any Legislature in India;
- (iii) any court, tribunal or other judicial authority in India;

**"Indian work"** means a literary, dramatic or musical work,-

- (i) the author of which is a citizen of India; or
- (ii) which is first published in India; or
- (iii) the author of which, in the case of an unpublished work, is, at the time of the making of the work, a citizen of India.

**"Infringing copy"** means,-

- (i) in relation to a literary, dramatic, musical or artistic work, a reproduction thereof otherwise than in the form of a cinematographic film;
- (ii) in relation to a cinematographic film, a copy of the film made on any medium by any means;
- (iii) in relation to a sound recording, any other recording embodying the same sound recording, made by any means;

- (iv) in relation to a programme or performance in which such a broadcast reproduction right or a performer's right subsists under the provisions of this Act, the sound recording or a cinematographic film of such programme or performance, if such reproduction, copy or sound recording is made or imported in contravention of the provisions of this Act;

**"Musical work"** means a work consisting of music and includes any graphical notation of such work but does not include any words or any action intended to be sung, spoken or performed with the music;

**"Performance"**, in relation to performer's right, means any visual or acoustic presentation made live by one or more performers;

**"Performer"** includes an actor, singer, musician, dancer, acrobat, juggler, conjurer, snake charmer, a person delivering a lecture or any other person who makes a performance;

"Provided that in a cinematograph film a person whose performance is casual or incidental in nature and, in the normal course of the practice of the industry, is not acknowledged anywhere including in the credits of the film shall not be treated as a performer except for the purpose of clause (b) of section 38B;"

**"Reprography"** means the making of copies of a work, by photo-copying or similar means;

**"Rights Management Information"** means,—

- (a) the title or other information identifying the work or performance;
- (b) the name of the author or performer;
- (c) the name and address of the owner of rights;
- (d) terms and conditions regarding the use of the rights; and
- (e) any number or code that represents the information referred to in sub-clauses (a) to (d),

but does not include any device or procedure intended to identify the user;

**"Sound recording"** means a recording of sounds from which such sounds may be produced regardless of the medium on which such recording is made or the method by which the sounds are produced;

**"Visual recording"** means the recording in any medium, by any method including the storing of it by any electronic means, of moving images or of the representations thereof, from which they can be perceived, reproduced or communicated by any method;

**"Work"** means any of the following works, namely:-

- a literary, dramatic, musical or artistic work;
- a cinematograph film;
- a sound recording.

### Meaning of Copyright

Section 14 of the Act defines the term Copyright as to mean the exclusive right to do or authorise the doing of the following acts in respect of a work or any substantial part thereof, namely

#### ***Copyright in the case of literary, dramatic or musical work:***

- (i) reproducing the work in any material form which includes storing of it in any medium by electronic means;

- (ii) issuing copies of the work to the public which are not already in circulation;
- (iii) performing the work in public or communicating it to the public;
- (iv) making any cinematograph film or sound recording in respect of the work;
- (v) making any translation or adaptation of the work. Further any of the above mentioned acts in relation to work can be done in the case of translation or adaptation of the work.

***Copyright in the case of a computer programme:***

- (i) to do any of the acts specified in respect of a literary, dramatic or musical work; and
- (ii) to sell or give on commercial rental or offer for sale or for commercial rental any copy of the computer programme. However, such commercial rental does not apply in respect of computer programmes where the programme itself is not the essential object of the rental.

***Copyright in the case of artistic work:***

- (i) to reproduce the work in any material form including—
  - (A) the storing of it in any medium by electronic or other means; or
  - (B) depiction in three-dimensions of a two-dimensional work; or
  - (C) depiction in two-dimensions of a three-dimensional work;”;
- (ii) communicating the work to the public;
- (iii) issuing copies of work to the public which are not already in existence;
- (iv) including work in any cinematograph film;
- (v) Making adaptation of the work, and to do any of the above acts in relation to an adaptation of the work.

***Copyright in the case of cinematograph film:***

- (i) to make a copy of the film, including—
  - (A) a photograph of any image forming part thereof; or
  - (B) storing of it in any medium by electronic or other means;”;
- (ii) to sell or give on commercial rental or offer for sale or for such rental, any copy of the film;
- (iii) to communicate the film to the public.

***Copyright in the case of sound recording:***

- (i) to make any other sound recording embodying it “including storing of it in any medium by electronic or other means”;
- (ii) to sell or give on commercial rental or offer for sale or for such rental, any copy of the sound recording;
- (iii) to communicate the sound recording to the public.

### **Who is an author?**

*In the case of a literary or dramatic work the author, i.e., the person who creates the work.*

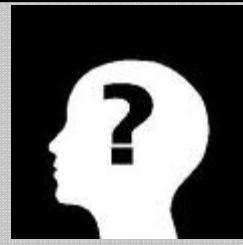
*In the case of a musical work, the composer.*

*In the case of a cinematograph film, the producer.*

*In the case of a sound recording, the producer.*

*In the case of a photograph, the photographer.*

*In the case of a computer generated work, the person who causes the work to be created.*



### **TERM OF COPYRIGHT**

Sections 22-29 deal with term of copyright in respect of published literary, dramatic, musical and artistic works; anonymous and pseudonymous; posthumous, photographs, cinematograph films, sound recording, Government works, works of PSUs and works of international organisations.

Literary, dramatic, musical or artistic works enjoy copyright protection for the life time of the author plus 60 years beyond i.e. 60 years after his death. In the case of joint authorship which implies collaboration of two or more authors in the production of the work, the term of copyright is to be construed as a reference to the author who dies last.

In the case of copyright in posthumous, anonymous and pseudonymous works, cinematograph films, sound recordings, works of Government, public undertaking and international organisations, the term of protection is 60 years from the beginning of the calendar year next following the year in which the work has been first published.

The Copyright (Amendment) Act, 1994 has given special right to every broad-casting organisation known as broadcast reproduction right in respect of its broadcasts. This right is to be enjoyed by every broadcasting organisation for a period of twenty-five years from the beginning of the calendar year next following the year in which the broadcast is made. In terms of Copyright (Amendment) Act, 1999 if any performer appears or engages in any performance, he has a special right in relation to such performance called performers right to be enjoyed for a period of fifty years.

### **COPYRIGHT BOARD**

Section 11 of the Act provides for the establishment of the Copyright Board and empowers the Central Government to constitute the same consisting of a Chairman and two other members. The Chairman of the Copyright Board shall be a person who is, or has been, a Judge of a High Court or is qualified for appointment as a Judge of a High Court. The Central Government may after consultation with the Chairman of the Copyrights Board, appoint a Secretary to the Copyright Board and such other officers and employees as may be considered necessary for the efficient discharge of the functions of the Copyright Board.

### **Functions of the Copyright Board**

The main functions of the Copyright Board are as under:

1. Settlement of disputes as to whether copies of any literary, dramatic or artistic work or records are issued to the public in sufficient numbers.

2. Settlement of disputes as to whether the term of copyright for any work is shorter in any other country than that provided for that work under the Act.
3. Settlement of disputes with respect to assignment of copyright as dealt with in Section 19A.
4. Granting of compulsory licences in respect of Indian works withheld from public.
5. Granting of compulsory licence to publish unpublished Indian works.
6. Granting of compulsory licence to produce and publish translation of literary and dramatic works.
7. Granting of compulsory licence to reproduce and publish literary, scientific or artistic works for certain purposes.
8. Determination of royalties payable to the owner of copyright.
9. Determination of objection lodged by any person as to the fees charged by Performing Rights Societies.
10. Rectification of Register on the application of the Registrar of Copyright or of any person aggrieved.

The Copyright Board has no powers to limit the user of copyright to any particular territorial area. An appeal against orders passed by the Copyright Board except under Section 6 lies to the High Court within whose jurisdiction the appellant resides or carries on business.

## **ASSIGNMENT OF COPYRIGHT**

Section 18 of the Copyright Act provides that the owner of the copyright in an existing work or the prospective owner of the copyright in a future work may assign to any person the copyright either wholly or partially and either generally or subject to limitations and either for the whole term of the copyright or any part thereof.

However, in case of the assignment of copyright in any future work, the assignment shall take effect only when the work comes into existence. No such assignment shall be applied to any medium or mode of exploitation of the work which did not exist or was not in commercial use at the time when the assignment was made, unless the assignment specifically referred to such medium or mode of exploitation of the work:

However, the author of the literary or musical work included in a cinematograph film shall not assign or waive the right to receive royalties to be shared on an equal basis with the assignee of copyright for the utilization of such work in any form other than for the communication to the public of the work along with the cinematograph film in a cinema hall, except to the legal heirs of the authors or to a copyright society for collection and distribution and any agreement to contrary shall be void.

The author of the literary or musical work included in the sound recording but not forming part of any cinematograph film shall not assign or waive the right to receive royalties to be shared on an equal basis with the assignee of copyright for any utilization of such work except to the legal heirs of the authors or to a collecting society for collection and distribution and any assignment to the contrary shall be void.

It may be noted that assignee in respects the assignment of the copyright in any future work includes the legal representatives of the assignee, if the assignee dies before the work comes into existence.

## **Mode of assignment**

Section 19 of the Act provides that an assignment of the copyright in any work should be in writing signed by the assignor or by his duly authorised agent. The assignment of copyright in any work required to identify such work, and also specify the rights assigned; the duration; territorial extent of such assignment; the

amount of royalty and any other consideration payable to the author or his legal heirs during the currency of the assignment and the assignment subject to revision, extension or termination on terms mutually agreed upon by the parties.

Where the assignee does not exercise the rights assigned to him under any of the other sub- sections of this section within a period of one year from the date of assignment, the assignment in respect of such rights shall be deemed to have lapsed after the expiry of the said period unless otherwise specified in the assignment.

The assignment of copyright in any work contrary to the terms and conditions of the rights already assigned to a copyright society in which the author of the work is a member is void.

The Assignment of copyright in any work to make a cinematograph film does not affect the right of the author of the work to claim an equal share of royalties and consideration payable in case of utilization of the work in any form other than for the communication to the public of the work, along with the cinematograph film in a cinema hall.

The assignment of the copyright in any work to make a sound recording which does not form part of any cinematograph film does not affect the right of the author of the work to claim an equal share of royalties and consideration payable for any utilization of such work in any form.

## LICENCES

Chapter VI containing Sections 30-32B deal with licences. Section 30 deals with licences by owners of copyright; Section 30A contains provisions regarding application of Sections 19 and 19A; section 31 provides for compulsory licence in works withheld from public; Section 31A deals with compulsory licences in unpublished Indian works; Section 31B deals with Compulsory Licence for the benefit of disabled; Section 31C deals with statutory licence for cover versions; Section 31D deals with statutory licence for broadcasting of literary and musical works and sound recording; Section 32 deals with licences to produce and publish translations; Section 32A provides for licence to reproduce and publish works for certain purposes; and Section 32B deals with termination of licences.

### Licences by Owners of Copyright

Section 30 of the Act empowers the owner of the copyright in any existing work or the prospective owner of the copyright in any future work to grant any interest in the right by licence in writing by him or by his duly authorised agent. However, in the case of a licence relating to copyright in any future work, the licence shall take effect only when the work comes into existence. Explanation to this section clarifies that where a person to whom a licence relating to copyright in any future work is granted, dies before the work comes into existence, his legal representatives shall, in the absence of any provision to the contrary in the licence, be entitled to the benefit of the licence.

### Compulsory Licence in Works Withheld from Public

Section 31 provides that if at any time during the term of copyright in any Indian work which has been published or performed in public, a complaint is made to the Copyright Board that the owner of copyright in the work has refused to re-publish or allow the re-publication of the work or has refused to allow the performance in public of the work, and by reason of such refusal the work is withheld from the public or has refused to allow communication to the public by broadcast of such work or in the case of a sound recording; the work recorded in such sound recording, on terms which the complainant considers reasonable, the Copyright Board, after giving to the owner of the copyright in the work a reasonable opportunity of being heard and after holding such inquiry as it may deem necessary, may, if it is satisfied that the grounds for

such refusal are not reasonable, direct the Registrar of Copyrights to grant to the complainant a licence to republish the work, perform the work in public or communicate the work to the public by broadcast, subject to payment to the owner of the copyright of such compensation and subject to such other terms and conditions as the Copyright Board may determine.

#### ***Compulsory licence in unpublished “or published works***

Section 31A of the Act provides that in the case of any unpublished work or any work published or communicated to the public and the work is withheld from the public in India, the author is dead or unknown or cannot be traced, or the owner of the copyright in such work cannot be found, any person may apply to the Copyright Board for a licence to publish or communicate to the public such work or a translation thereof in any language.

Before making an application to the Copyright Board, the applicant required to publish his proposal in one issue of a daily newspaper in the English language having circulation in the major part of the country and where the application is for the publication of a translation in any language, also in one issue of any daily newspaper in that language.

The Copyright Board after holding such inquiry as may be prescribed, direct the Registrar of Copyrights to grant to the applicant a licence to publish the work or a translation thereof in the language mentioned in the application subject to the payment of such royalty and subject to such other terms and conditions as the Copyright Board may determine, and thereupon the Registrar of Copyrights shall grant the licence to the applicant in accordance with the direction of the Copyright Board.

#### ***Compulsory licence for benefit of disabled***

Section 31B (1) provides that any person working for the benefit of persons with disability on a profit basis or for business may apply to the Copyright Board in prescribed manner for a compulsory licence to publish any work in which copyright subsists for the benefit of such persons, in a case to which clause (zb) of sub-section (1) of section 52 does not apply and the Copyright Board shall dispose of such application as expeditiously as possible and endeavour shall be made to dispose of such application within a period of two months from the date of receipt of the application.

The Copyright Board may on receipt of an application inquire, or direct such inquiry as it considers necessary to establish the credentials of the applicant and satisfy itself that the application has been made in good faith and a compulsory licence needs to be issued to make the work available to the disabled, it may direct the Registrar of Copyrights to grant to the applicant such a licence to publish the work.

It may be noted that clause (zb) of sub-section (1) of section 52 provides that the adaptation, reproduction, issue of copies or communication to the public of any work in any accessible format, by—

- (i) any person to facilitate persons with disability to access to works including sharing with any person with disability of such accessible format for private or personal use, educational purpose or research; or
- (ii) any organisation working for the benefit of the persons with disabilities in case the normal format prevents the enjoyment of such works by such persons:

However, the copies of the works in such accessible format are made available to the persons with disabilities on a non-profit basis but to recover only the cost of production and the organization ensure that the copies of works in such accessible format are used only by persons with disabilities and takes reasonable steps to prevent its entry into ordinary channels of business.

It may be noted that “any organization” includes and organization registered under section 12A of the Income-tax Act, 1961 and working for the benefit of persons with disability or recognized under Chapter X of the Persons with Disabilities (Equal Opportunities, Protection or Rights and full Participation) Act, 1995 or receiving grants from the government for facilitating access to persons with disabilities or an educational institution or library or archives recognized by the Government.”.

### ***Statutory Licence for cover versions***

Section 31C (1) provides that any person desirous of making a cover version, being a sound recording in respect of any literary, dramatic or musical work, where sound recordings of that work have been made by or with the licence or consent of the owner of the right in the work, may do so subject to the provisions of this section. However, such sound recordings shall be in the same medium as the last recording, unless the medium of the last recording is no longer in current commercial use.

The person making the sound recordings required to give prior notice of his intention to make the sound recordings in the manner as may be prescribed, and provide in advance copies of all covers or labels with which the sound recordings are to be sold, and pay in advance, to the owner of rights in each work royalties in respect of all copies to be made by him, at the rate fixed by the Copyright Board .

It may be noted that such sound recordings shall not be sold or issued in any form of packaging or with any cover or label which is likely to mislead or confuse the public as to their identity, and in particular shall not contain the name or depict in any way any performer of an earlier sound recording of the same work or any cinematograph film in which such sound recording was incorporated and, further, shall state on the cover that it is a cover version made under this section.

The person making such sound recordings shall not make any alteration in the literary or musical work which has not been made previously by or with the consent of the owner of rights, or which is not technically necessary for the purpose of making the sound recordings. However, such sound recordings shall not be made until the expiration of five calendar years after the end of the year in which the first sound recordings of the work was made.

It may be noted that cover version means a sound recording made in accordance with this Section 31C of the Act.

### ***Statutory licence for broadcasting of literary and musical works and sound recording***

Section 31D provides that any broadcasting organisation desirous of communicating to the public by way of a broadcast or by way of performance of a literary or musical work and sound recording which has already been published may do so subject to the fulfillment of prescribed conditions.

The broadcasting organisation required to give prior notice in prescribed manner of its intention to broadcast the work stating the duration and territorial coverage of the broadcast, and pay to the owner of rights in each work royalties in the manner and at the rate fixed by the Copyright Board.

The rates of royalty for radio broadcasting shall be different from television broadcasting and the copyright Board shall fix separate rates for radio broadcasting and television broadcasting and the broadcasting organisation to pay an advance to the owners of rights.

The broadcasting organisation required to maintain such records and books of account, and render to the owners of rights such reports and accounts; and allow the owner of rights or his duly authorised agent or representative to inspect all records and books of account relating to such broadcast in prescribed manner.

### **Licence to Produce and Publish Translations**

Section 32 entitles any person to apply to the Copyright Board for a licence to produce and publish a translation of a literary or dramatic work in any language after a period of seven years from the first publication of the work. However, in respect of teaching, scholarship or research Section 32(1A) allows any person to apply to the Copyright Board for a licence to produce and publish a translation, in printed or analogous forms of reproduction, of a literary or dramatic work, other than an Indian work, in any language in general use in India after a period of three years from the first publication of such work. Further, where such translation is in a language not in general use in any developed country, such application may be made after a period of one year from such publication.

### **Termination of Licence**

Section 32B of the Act deals with termination of licences and provides that if at any time after the granting of a licence, the owner of the copyright in the work or any person authorised by him publishes a translation of such work in the same language and which is substantially the same in content at a price reasonably related to the price normally charged in India for the translation of works of the same standard on the same or similar subject, the licence so granted shall be terminated. However, such termination shall take effect only after the expiry of a period of three months from the date of service of a notice in the prescribed manner on the person holding such licence by the owner of the right of translation intimating the publication of the translation.

### **COPYRIGHT SOCIETIES**

Section 33(1) prohibits any person or association of persons to commence or, carry on the business of issuing or granting licences in respect of any work in which copyright subsists on respect or in respect of any other rights conferred by the Act.

However, owner of copyright in his individual capacity, continue to have the right to grant licences in respect of his own works consistent with his obligations as a member of the registered copyright society. The business of issuing or granting license in respect of literary, dramatic, musical and artistic works incorporated in a cinematograph films or sound recordings shall be carried out only through a copyright society duly registered under the Act.

Sub section (3) of Section 33 provides that Central Government registers association of persons as a copyright society after taking into account the following factors:

- in the interests of the authors and other owners of rights;
- the interest and convenience of the public and in particular of the groups of persons who are most likely to seek licences in respect of the relevant rights and
- the ability and professional competence of the applicants.

As per Sub section (3A) of Section 33 registration granted to a copyright society under sub-section (3) mentioned above shall be for a period of five years and may be renewed from time to time before the end of every five years on a request in the prescribed form and the Central Government may renew the registration after considering the report of Registrar of Copyrights on the working of the copyright society. However, the renewal of the registration of a copyright society shall be subject to the continued collective control of the copyright society being shared with the authors of works in their capacity as owners of copyright or of the right to receive royalty.

Central Government if satisfied that a copyright society is being managed in a manner detrimental to the

interests of "authors and other owners of right" concerned, cancel the registration of such society after such inquiry as may be prescribed.

### **Tariff scheme by copyright society**

Section 33A of the Act provides that every copyright society shall publish its Tariff Scheme in the prescribed manner. Any person who is aggrieved by the tariff scheme may appeal to the Copyright Board and the Board after holding inquiry makes such orders as may be required to remove any unreasonable element, anomaly or inconsistency therein.

### **Administration of rights of owner by copyright society**

Section 34 of the Act empowers a copyright society to accept exclusive authorisation from an author and other owners of right to administer any right in any work by issue of licences or collection of licence fees or both. Such authorization can be withdrawn by an author and other owners of right.

Copyright society is competent to enter into agreement with any foreign society or organisation administering rights corresponding to rights under the Indian Copyright Act to entrust to such foreign society or organisation the administration in any foreign country of rights administered by the said copyright society in India, or for administering in India the rights administered in a foreign country by such foreign society or organisation.

Copyright Society empower to—

- (i) issue licences under section 30 in respect of any rights under this Act;
- (ii) collect fees in pursuance of such licences;
- (iii) distribute such fees among author and other owners of right after making deductions for its own expenses;
- (iv) perform any other functions consistent which the provisions of section 35.

### **Control over the copyright society by the author and other owners of right**

As per Section 35 every copyright society is subject to the collective control of the owners of rights it administers. It does not includes administered by a foreign society or organisation .

Every copyright society shall have a governing body with such number of persons elected from among the members of the society consisting of equal number of authors and owners of work for the purpose of the administration of the society. All members of copyrights society shall enjoy equal membership rights and there shall be no discrimination between authors and owners of rights in the distribution of royalties.

## **RIGHTS OF BROADCASTING ORGANISATION AND PERFORMERS**

Chapter VIII of the Act containing Section 37-39A deals with rights of broadcasting organisations and of performers.

### **Broadcast reproduction right**

Section 37 entitles every broadcasting organisation to have a special right to be known as "broadcast reproduction right" in respect of its broadcasts for twenty-five years from the beginning of the calendar year next following the year in which the broadcast is made.

As per sub section (3) of section 37 during the continuance of a broadcast reproduction right in relation to any broadcast, any person who, without the licence of the owner of the right does any of the following acts of

the broadcast or any substantial part thereof,-

- (a) re-broadcasts the broadcast; or
- (b) causes the broadcast to be heard or seen by the public on payment of any charges; or
- (c) makes any sound recording or visual recording of the broadcast; or
- (d) makes any reproduction of such sound recording or visual recording where such initial recording was done without licence or, where it was licensed, for any purpose not envisaged by such licence; or
- (e) sells or gives on commercial rental or offer for sale or for such rental, any such sound recording or visual recording referred to in clause (c) or clause (d) and subject to the provisions of Section 39 deemed to have infringed broadcast reproduction right..

### **Performer's right**

Section 38 provides that where any performer appears or engages in any performance, he shall have a special right to be known as the "performer's right" in relation to such performance. The performer's right subsist until fifty years from the beginning of the calendar year next following the year in which the performance is made.

### **Exclusive Right of Performer**

As per section 38A without prejudice to the rights conferred on authors, the performer's right which is an exclusive right subject to the provisions of the Act to do or authorise for doing any of the following acts in respect of the performance or any substantial part thereof, namely:—

- (a) to make a sound recording or a visual recording of the performance, including—
  - (i) reproduction of it in any material form including the storing of it in any medium by electronic or any other means;
  - (ii) issuance of copies of it to the public not being copies already in circulation;
  - (iii) communication of it to the public;
  - (iv) selling or giving it on commercial rental or offer for sale or for commercial rental any copy of the recording;
- (b) to broadcast or communicate the performance to the public except where the performance is already broadcast.

It may be noted that once a performer has, by written agreement, consented to the incorporation of his performance in a cinematograph film he shall not, in the absence of any contract to the contrary, object to the enjoyment by the producer of the film of the performer's right in the same film. However, the performer shall be entitled for royalties in case of making of the performances for commercial use.

### **Moral Right of Performer**

Section 38B of Act provides that the performer of a performance shall, independently of his right after assignment, either wholly or partially of his right, have the right to claim to be identified as the performer of his performance except where omission is dictated by the manner of the use of the performance; and to restrain or claim damages in respect of any distortion, mutilation or other modification of his performance that would be prejudicial to his reputation.

It may be noted that mere removal of any portion of a performance for the purpose of editing, or to fit the recording within a limited duration, or any other modification required for purely technical reasons shall not be deemed to be prejudicial to the performer's reputation.

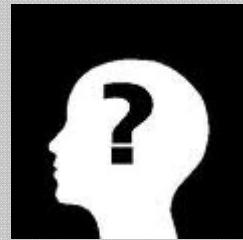
### **Acts not constituting Infringement of Broadcast Reproduction Right and Performers Right**

Section 39 stipulates situations in which no broadcast reproduction right or performers right shall be deemed to be infringed. These include:

- (a) the making of any sound recording or visual recording for the private use of the person making such recording, or solely for purposes of bona fide teaching or research; or
- (b) the use, consistent with fair dealing of excerpts of a performance or of a broadcast in the reporting of current events or for bona fide review, teaching or research; or
- (c) such other acts, with any necessary adaptations and modifications, which do not constitute infringement of copyright under Section 52.

#### ***What are the moral rights of an author?***

*The author of a work has the right to claim authorship of the work and to restrain or claim damages in respect of any distortion, mutilation, modification or other acts in relation to the said work which is done before the expiration of the term of copyright if such distortion, mutilation, modification or other act would be prejudicial to his honour or reputation. Moral rights are available to the authors even after the economic rights are assigned.*



## **INTERNATIONAL COPYRIGHT**

### **Copyright Protection to Foreign Works**

The Copyright Act applies only to works first published in India, irrespective of the nationality of the author. However Section 40 of the Act empowers the Government of India to extend the benefits of all or any of the provisions of the Act to works first published in any foreign country. The benefits granted to foreign works will not extend beyond what is available to the works in the home country and that too on a reciprocal basis i.e. the foreign country must grant similar protection to works entitled to copyright under the Act. The term of Copyright in India to the foreign work, will not exceed that conferred by the foreign country.

Government of India has passed the International Copyright Order, 1958. According to this order any work first published in any country which is a member of the Berne Convention or the Universal Copyright Convention will be accorded the same treatment as if it was first published in India.

#### ***Conditions of Copyright Protection***

The following are the requisites for conferring copyright protection to works of international organisations:

- (a) The work must be made or first published by or under the direction or control of the International Organisation.
- (b) There should be no copyright in the work in India at the time of making or on the first publication of the work.

- (c) If the work is published in pursuance of an agreement with the author, such agreement should not reserve the author any copyright in the work or any copyright in the work should belong to the organisation.

### **Power of Central Government to apply Chapter VIII to Broadcasting Organisations and Performers in Certain other Countries**

Section 40A inserted by the Copyright (Amendment) Act, 1999 provides that subject to the satisfaction of Central Government that a foreign country (other than a country with which India has entered into a treaty or which is a party to a Convention relating to rights of broadcasting organisations and performers to which India is a party) has made or has undertaken to make such provisions, if any, as it appears to the Central Government expedient to require, for the protection in that foreign country, of the rights of broadcasting organisations and performers as is available under this Act, it may, by order, published in the Official Gazette, direct that the provisions of Chapter VIII shall apply:

- (a) to broadcasting organizations whose headquarters is situated in a country to which the order relates or, the broadcast was transmitted from a transmitter situated in a country to which the order relates as if the headquarters of such organisation were situated in India or such broadcast were made from India;
- (b) to performances that took place outside India to which the order relates in like manner as if they took place in India;
- (c) to performances that are incorporated in a sound recording published in a country to which the order relates as if it were published in India;
- (d) to performances not fixed on a sound recording broadcast by a broadcasting organisation the headquarters of which is located in a country to which the order relates or where the broadcast is transmitted from a transmitter which is situated in a country to which the order relates as if the headquarters of such organisation were situated in India or such broadcast were made from India.

Section 40A(2) also provides that the order so made by the Central Government may provide that:

- (i) the provisions of Chapter VIII shall apply either generally or in relation to such class or classes of broadcasts or performance or such other class or classes of cases as may be specified in the order;
- (ii) the term of the rights of broadcasting organisations and performers in India shall not exceed such term as is conferred by the law of the country to which the order relates;
- (iii) the enjoyment of the rights conferred by Chapter VIII shall be subject to the accomplishment of such conditions and formalities, if any, as may be specified in that order;
- (iv) chapter VIII or any part thereof shall not apply to broadcast and performances made before the commencement of the order or that Chapter VIII or any part thereof shall not apply to broadcasts and performances broadcast or performed before the commencement of the order;
- (v) in case of ownership of rights of broadcasting organisations and performers, the provisions of Chapter VIII shall apply with such exceptions and modifications as the Central Government, may having regard to the law of the foreign country, consider necessary.

### **Power to Restrict Rights of Foreign Broadcasting Organisations and Performers**

Section 42A provides that if it appears to the Central Government that a foreign country does not give or has not undertaken to give adequate protection to rights of broadcasting organisations or performers, the Central Government may, by order, published in the Official Gazette, direct that such of the provisions of this Act as

confer right to broadcasting organizations or performers, as the case may be, shall not apply to broadcasting organizations or performers whereof are based or incorporated in such foreign country or are subjects or citizens of such foreign country and are not incorporated or domiciled in India, and thereupon those provisions shall not apply to such Broadcasting organizations or performers.

## REGISTRATION OF COPYRIGHT

Chapter X of the Act containing Sections 44- 50A deals with various aspects of registration of copyright.

The mechanism of registration of copyright has been contemplated under Section 44 of the Act. It is evident from the provisions of the aforesaid section that registration of the work under the Copyright Act is not compulsory and is not a condition precedent for maintaining a suit for damages, if somebody infringes the copyright. Sections 44 and 45 of the Copyright Act are only enabling provisions and do not affect the common law right to sue for infringement of copyright. An action for infringement can be brought even if the registration has not been done. The only effect of registration is that it is the *prima facie* evidence of the particulars entered in the register.

The Register of Copyrights is to be maintained by the Copyright Office to enter the names or titles of works and the names and addresses of authors, publishers and owners of copyright. The Register of Copyrights is to be kept in Six parts, namely, Part I Literary works other than computer programmes, tables and compilations including computer data bases and dramatic works; Part II Musical works; Part III Artistic works; Part IV Cinematograph films; Part V Sound Recording; and Part VI Computer programmes, tables and compilations including computer data bases.

## INFRINGEMENT OF COPYRIGHT

Copyright protection gives exclusive rights to the owners of the work to reproduce the work enabling them to derive financial benefits by exercising such rights. If any person without authorisation from the owner exercises these rights in respect of the work which has copyright protection it constitutes an infringement of the copyright. If the reproduction of the work is carried out after the expiry of the copyright term it will not amount to an infringement.

Section 51 of the Act contemplates situation in which a copyright shall be deemed to be infringed. This Section says that a copyright is infringed when any person without a licence granted by the owner of the copyright or the Registrar of Copyright or in contravention of the conditions of a licence so granted or of any condition imposed by a competent authority does

- (1) anything for which the exclusive right is conferred upon the owner of the copyright, or
- (2) permits for profit any place to be used for the communication of the work to public where such a communication constitutes an infringement of the copyright in the work, unless he was not aware and had no reasonable ground for believing that such communication would be an infringement of copyright.
- (3) when any person (i) makes for sale or hire or lets for hire or by way of trade display or offers for sale or hire, or (ii) distributes either for the purpose of trade or to such an extent as to affect prejudicially the owner of the copyright, or (iii) by way of trade, exhibits in public, or (iv) imports into India any infringing copies of the work.

However, import of one copy of any work is allowed for private and domestic use of the importer. Explanation to Section 51 clarifies that the reproduction of literary, dramatic musical or artistic work in the form of cinematograph film shall be deemed to be an infringing copy.

### **Which are the common copyright infringements?**

The following are some of the commonly known acts involving infringement of copyright:

- Making infringing copies for sale or hire or selling or letting them for hire;
- Permitting any place for the performance of works in public where such performance constitutes infringement of copyright;
- Distributing infringing copies for the purpose of trade or to such an extent so as to affect prejudicially the interest of the owner of copyright ;
- Public exhibition of infringing copies by way of trade; and
- Importation of infringing copies into India.



### **Statutory Exceptions**

Certain exceptions to infringement have been stipulated by the Copyright Act. The object of these exceptions is to enable the reproduction of the work for certain public purposes, and for encouragement of private study, research and promotion of education. The list of acts which do not constitute infringement of copyright has been provided under Section 52 of the Act. These include

(i) A fair dealing with any work, not being a computer programme, for the purposes of—

- private or personal use, including research;
- criticism or review, whether of that work or of any other work;
- reporting of current events and current affairs, including the reporting of a lecture delivered in public.

It may be noted that storing of any work in any electronic medium including the incidental storage of any computer programme which is not itself an infringing copy for the said purposes, shall not constitute infringement of copyright.

(ii) The making of copies or adaptation of a computer programme by the lawful possessor of a copy of such computer programme, from such copy in order to utilise the computer programme for the purposes for which it was supplied; or to make back-up copies purely as a temporary protection against loss, destruction or damage in order only to utilise the computer programme for the purpose for which it was supplied.

(iii) the doing of any act necessary to obtain information essential for operating inter-operability of an independently created computer programme with other programmes by a lawful possessor of a computer programme provided that such information is not otherwise readily available.

(iv) the observation, study or test of functioning of the computer programme in order to determine the ideas and principles which underline any elements of the programme while performing such acts necessary for the functions for which the computer programme was supplied.

(v) the making of copies or adaptation of the computer programme from a personally legally obtained copy for non-commercial personal use.

(vi) the transient or incidental storage of a work or performance purely in the technical process of electronic transmission or communication to the public.

(vii) transient or incidental storage of a work or performance for the purpose of providing electronic links, access or integration, where such links, access or integration has not been expressly prohibited by the right

holder, unless the person responsible is aware or has reasonable grounds for believing that such storage is of an infringing copy.

It may be noted that if the person responsible for the storage of the copy has received a written complaint from the owner of copyright in the work, complaining that such transient or incidental storage is an infringement, such person responsible for the storage shall refrain from facilitating such access for a period of twenty-one days or till he receives an order from the competent court refraining from facilitating access and in case no such order is received before the expiry of such period of twenty-one days, he may continue to provide the facility of such access.

(viii) the reproduction of any work for the purpose of a judicial proceeding or for the purpose of a report of a judicial proceeding.

(ix) the reproduction or publication of any work prepared by the Secretariat of a Legislature or, where the Legislature consists of two Houses, by the Secretariat of either House of the Legislature, exclusively for the use of the members of that Legislature.

(x) the reproduction of any work in a certified copy made or supplied in accordance with any law for the time being in force;

(xi) the reading or recitation in public of reasonable extracts from a published literary or dramatic work.

(xii) the publication in a collection, mainly composed of non-copyright matter, bona fide intended for instructional use, and so described in the title and in any advertisement issued by or on behalf of the publisher, of short passages from published literary or dramatic works, not themselves published for such use in which copyright subsists. However, not more than two such passages from works by the same author are published by the same publisher during any period of five years.

In the case of a work of joint authorship, references in this clause to passages from works shall include references to passages from works by any one or more of the authors of those passages or by any one or more of those authors in collaboration with any other person.

(xiii) the reproduction of any work—

- by a teacher or a pupil in the course of instruction; or
- as part of the questions to be answered in an examination; or
- in answers to such questions.

(xiv) the performance, in the course of the activities of an educational institution, of a literary, dramatic or musical work by the staff and students of the institution, or of a cinematograph film or a sound recording if the audience is limited to such staff and students, the parents and guardians of the students and persons connected with the activities of the institution or the communication to such an audience of a cinematograph film or sound recording.

(xv) the causing of a recording to be heard in public by utilising it,-

- in an enclosed room or hall meant for the common use of residents in any residential premises (not being a hotel or similar commercial establishment) as part of the amenities provided exclusively or mainly for residents therein; or
- as part of the activities of a club or similar organisation which is not established or conducted for profit;
- as part of the activities of a club, society or other organisation which is not established or conducted for profit.

(xvi) the performance of a literary, dramatic or musical work by an amateur club or society, if the performance is given to a non-paying audience, or for the benefit of a religious institution.

(xvii) the reproduction in a newspaper, magazine or other periodical of an article on current economic, political, social or religious topics, unless the author of such article has expressly reserved to himself the right of such reproduction.

(xviii) the storing of a work in any medium by electronic means by a noncommercial public library, for preservation if the library already possesses a non-digital copy of the work.

(xix) the making of not more than three copies of a book (including a pamphlet, sheet of music, map, chart or plan) by or under the direction of the person in charge of a non-commercial public library for the use of the library if such book is not available for sale in India;

(xx) the reproduction, for the purpose of research or private study or with a view to publication, of an unpublished literary, dramatic or musical work kept in a library, museum or other institution to which the public has access.

However, where the identity of the author of any such work or, in the case of a work of joint authorship, of any of the authors is known to the library, museum or other institution, as the case may be, the provisions of this clause shall apply only if such reproduction is made at a time more than sixty years from the date of the death of the author or, in the case of a work of joint authorship, from the death of the author whose identity is known or, if the identity of more authors than one is known from the death of such of those authors who dies last;

(xxi) the reproduction or publication of-

- any matter which has been published in any Official Gazette except an Act of a Legislature;
- any Act of a Legislature subject to the condition that such Act is reproduced or published together with any commentary thereon or any other original matter;
- the report of any committee, commission, council, board or other like body appointed by the Government if such report has been laid on the Table of the Legislature, unless the reproduction or publication of such report is prohibited by the Government;
- any judgement or order of a court, tribunal or other judicial authority, unless the reproduction or publication of such judgment or order is prohibited by the court, the tribunal or other judicial authority, as the case may be.

(xxii) the production or publication of a translation in any Indian language of an Act of a Legislature and of any rules or orders made thereunder-

- if no translation of such Act or rules or orders in that language has previously been produced or published by the Government; or
- where a translation of such Act or rules or orders in that language has been produced or published by the Government, if the translation is not available for sale to the public;
- however, such translation contains a statement at a prominent place to the effect that the translation has not been authorised or accepted as authentic by the Government.

(xxiii) the making or publishing of a painting, drawing, engraving or photograph of a work of architecture or the display of a work of architecture.

**(xxiv)** the making or publishing of a painting, drawing, engraving or photograph of a sculpture, or other artistic work failing under sub-clause (iii) of clause (c) of section 2, if such work is permanently situate in a public place or any premises to which the public has access.

**(xxv)** the inclusion in a cinematograph film of-

- any artistic work permanently situate in a public place or any premises to which the public has access; or
- any other artistic work, if such inclusion is only by way of background or is otherwise incidental to the principal matters represented in the film.

**(xxvi)** the use by the author of an artistic work, where the author of such work is not the owner of the copyright therein, of any mould, cast, sketch, plan, model or study made by him for the purpose of the work. However, he does not thereby repeat or imitate the main design of the work.

**“(xxvii)** the making of a three-dimensional object from a two-dimensional artistic work, such as a technical drawing, for the purposes of industrial application of any purely functional part of a useful device;

**(xxviii)** the reconstruction of a building or structure in accordance with the architectural drawings or plans by reference to which the building or structure was originally constructed . However, the original construction was made with the consent or licence of the owner of the copyright in such drawings and plans.

**(xxix)** in relation to a literary, “dramatic, artistic or” musical work recorded or reproduced in any cinematograph film the exhibition of such film after the expiration of the term of copyright therein .However, the provisions of sub-clause (ii) of clause (a), sub-clause (a) of clause (b) and clauses (d), (f), (g), (m) and (p) shall not apply as respects any act unless that act is accompanied by an acknowledgment-

- identifying the work by its title or other description; and
- unless the work is anonymous or the author of the work has previously agreed or required that no acknowledgement of his name should be made, also identifying the author.

**(xxx)** the making of an ephemeral recording, by a broadcasting organisation using its own facilities for its own broadcast by a broadcasting organisation of a work which it has the right to broadcast; and the retention of such recording for archival purposes on the ground of its exceptional documentary character.

**(xxxi)** the performance of a literary, dramatic or musical work or the communication to the public of such work or of a sound recording in the course of any *bona fide* religious ceremony or an official ceremony held by the Central Government or the State Government or any local authority. *However, religious ceremony including a marriage procession and other social festivities associated with a marriage.*

**“(xxxii)** the adaptation, reproduction, issue of copies or communication to the public of any work in any accessible format by any person to facilitate persons with disability to access to works including sharing with any person with disability of such accessible format for private or personal use, educational purpose or research; or any organisation working for the benefit of the persons with disabilities in case the normal format prevents the enjoyment of such works by such persons. However, the copies of the works in such accessible format are made available to the persons with disabilities on a non-profit basis but to recover only the cost of production and the organization shall ensure that the copies of works in such accessible format are used only by persons with disabilities and takes reasonable steps to prevent its entry into ordinary channels of business.

It may be noted that “any organization” includes and organization registered under section 12A of the Income-tax Act, 1961 and working for the benefit of persons with disability or recognized under Chapter X of the Persons with Disabilities (Equal Opportunities, Protection or Rights and full Participation) Act, 1995 or receiving grants from the government for facilitating access to persons with disabilities or an educational institution or library or archives recognized by the Government.”.

(xxxiii) the importation of copies of any literary or artistic work, such as labels, company logos or promotional or explanatory material, that is purely incidental to other goods or products being imported lawfully.

### **Remedies against Infringement of Copyright**

Section 55 provides for the civil remedies for infringement of copyright and entitles the owner of the copyright to all such remedies by way of injunction, damages, accounts and otherwise as may be conferred by law for the infringement of copyright. Section 54 defines the term owner of copyright. Section 58 entitles the owner of the copyright to initiate proceedings for the possession of infringing copies and other materials related thereto. In this context, the section clarifies that all infringing copies of any work in which copyright subsists and all plates used or intended to be used for the production of such infringing copies shall be deemed to be the property of the owner of the copyright.

### **Authors Special Rights**

Apart from remedies for infringement of copyright, the Act expressly provides for the protection of special rights of the author known as moral rights. Under Section 57 of the Act an author of copyright work can restrain or claim damages in respect of any distortion mutilation of the work or any other action in relation to the said work which would be prejudicial to his honour or reputation. These rights can be exercised even after the assignment of the copyright. They can be enforced by an action for breach of contract or confidence, a suit for defamation, or passing off as the case may be.

### **OFFENCES AND PENALTIES**

Chapter XIII of the Act containing Sections 63-70 deal with offences and penalties. Section 63 deals with offences of infringement of copyright or other rights conferred by the Copyright Act, 1957. This section makes, any person who knowingly infringes or abates the infringement of the copyright in a work or any other right conferred under the Act (except for resale share right in original copies), liable to imprisonment for a minimum period of six months which may extend to three years and with minimum fine of fifty thousand rupees which may extend upto rupees two lakhs. However, the court has been empowered to impose a sentence less than six months or a fine less than fifty thousand, if the infringement had not been made for gain in the course of trade or business. In such situations, the section requires the courts to mention adequate and special reasons in the judgement.

Section 63A deals with second and subsequent convictions and provides for imprisonment not less than one year extendable to three years and the fine not less than one lakh rupees, extendable to rupees two lakhs.

### **Power of Police to Seize Infringing Copies**

Section 64 of the Act empowers any Police Officer, not below the rank of a sub-inspector, to seize without warrant, all copies of the work and all plates used for the purpose of making infringing copies of the work, wherever they are found. However such Police Officer has to satisfy himself before such seizure, that an offence under Section 63 in respect of the infringement of copyright in any work has been, is being or is likely

to be committed. Further, such Police Officer has been put under obligation to produce before the Magistrate, as soon as practicable, all copies and plates so seized.

Any interested person may make an application to Magistrate, within fifteen days of such seizure, for restoring to him such copies and plates. Section 65 makes liable, any person, who knowingly makes or has in his possession, any plate for the purpose of making infringing copies of any work in which copyright subsists, to imprisonment which may extend to two years and also fine.

### **Protection of technological measures**

Section 65A provides that any person who circumvents an effective technological measure applied for the purpose of protecting any of the rights conferred by the Act, with the intention of infringing such rights, shall be punishable with imprisonment which may extend to two years and shall also be liable to fine.

The list of the acts not prevent any person from technological measure provided under sub-section (2) of section 65A. These include:

- doing anything referred to therein for a purpose not expressly prohibited by the Act. However, any person facilitating circumvention by another person of a technological measure for such a purpose shall maintain a complete record of such other person including his name, address and all relevant particulars necessary to identify him and the purpose for which he has been facilitated; or
- doing anything necessary to conduct encryption research using a lawfully obtained encrypted copy; or
- conducting any lawful investigation; or
- doing anything necessary for the purpose of testing the security of a computer system or a computer network with the authorisation of its owner; or operator; or
- doing anything necessary to circumvent technological measures intended for identification or surveillance of a user; or

taking measures necessary in the interest of national security.

### **Protection of Right of Management Information**

As per section 65B any person, who knowingly removes or alters any rights management information without authority, or distributes, imports for distribution, broadcasts or communicates to the public, without authority, copies of any work, or performance knowing that electronic rights management information has been removed or altered without authority, shall be punishable with imprisonment which may extend to two years and shall also be liable to fine:

Section 67 treats the making of false entries in register etc. for producing or tendering false entries, a punishable offence with imprisonment which may extend to one year or with fine or both.

Section 68 treats the making of false statement for the purpose of deceiving or influencing any officer or authority, a punishable offence with imprisonment upto one year or with fine or both.

Section 68A deals with penalty for contravention of Section 52A and provides that any person who publishes a sound recording or a video film in contravention of the provisions of Section 52A (particulars to be included in sound recording video film) shall be punishable with imprisonment which may extend to three years and shall also be liable to fine.

## **LESSON ROUND UP**

- Copyright is a well recognized form of property right which had its roots in the common law system and subsequently came to be governed by the national laws in each country. In India, the law relating to copyright is governed by the Copyright Act, 1957 which has been last amended in 2012.
- Copyright ensures certain minimum safeguards of the rights of authors over their creations.
- The Copyright (Amendment) Act 1992 has extended the period of copyright by another 10 years. Now literary, dramatic, musical or artistic works enjoy copyright protection for the life time of the author plus 60 years beyond i.e. 60 years after his death. In the case of joint authorship which implies collaboration of two or more authors in the production of the work, the term of copyright is to be construed as a reference to the author who dies last.
- The Act is now amended in 2012 with the object of making certain changes for clarity, to remove operational difficulties and also to address certain newer issues that have emerged in the context of digital technologies and the Internet.
- Section 18 of the Copyright Act provides for the assignment of copyright in an existing work as well as future work. In both the cases an assignment may be made of the copyright either wholly or partially and generally or subject to limitations and that too for the whole period of copyright or part thereof.
- Copyright protection gives exclusive rights to the owners of the work to reproduce the work enabling them to derive financial benefits by exercising such rights. If any person without authorisation from the owner exercises these rights in respect of the work which has copyright protection it constitutes an infringement of the copyright.
- Certain exceptions to infringement have been stipulated by the Copyright Act. The object of these exceptions is to enable the reproduction of the work for certain public purposes, and for encouragement of private study, research and promotion of education.
- The Copyright Act provides for the civil remedies for infringement of copyright and entitles the owner of the copyright to all such remedies by way of injunction, damages, accounts.

## **SELF TEST QUESTIONS**

1. Briefly explain the concept of copyright.
2. Discuss in detail the Copyright Board.
3. Discuss in detail the provisions relating to infringement of copyright.
4. Write short note on the following:
  - (i) Government work.
  - (ii) Term of Copyright.
5. Elaborate the provisions relating to certain exception to infringement have been stipulated by the Copyright Act.

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# INTELLECTUAL PROPERTY RIGHTS [GEOGRAPHICAL INDICATION OF GOODS (REGISTRATION AND PROTECTION) ACT, 1999]

## Section V

### LESSON OUTLINE

- Geographical Indication
- Registration of GI
- prohibits registration of certain geographical indications
- Application for Registration
- Prohibition of Registration of Geographical Indication as Trade Marks
- Duration of Registration
- Infringement of GI
- Assignment and Transmission

### LEARNING OBJECTIVES

Every region has its claim to fame. Each fame and reputation was carefully built up and painstakingly maintained by the masters of that region, combining the best of nature, man and traditionally handed over from one generation to the next for centuries. Gradually, a specific link between the goods and place of production evolved resulting in growth of geographical indications.

Geographical Indications of Goods are that aspect of industrial property which refers to a country or to a place situated therein as being the country or place of origin of that product. Typically, such a name conveys an assurance of quality and distinctiveness which is essentially attributable to the fact of its origin in that defined geographical locality, region or country.

The objective of the study is to thoroughly acclimatize the students with the law relating to Geographical Indication.

The Geographical Indication of Goods (Registration and Protection) Act, 1999 provides for the registration and better protection of geographical indications relating to goods. It extends to whole of India.

## **GEOGRAPHICAL INDICATIONS OF GOODS (REGISTRATION & PROTECTION) ACT, 1999**

### **Introduction**

Geographical Indications covered under Articles 22 to 24 of the WTO Trade Related Aspects of Intellectual Property Rights (TRIPS) Agreement, which was part of the Agreements concluding the Uruguay Round of GATT negotiations. India, as a member of the World Trade Organization (WTO), enacted the Geographical Indications of Goods (Registration & Protection) Act, 1999. In December 1999 and it has come into force with effect from 15th September 2003. This Act seeks to provide for the registration and better protection of geographical indications relating to goods in India. Examples of Indian Geographical Indications are Darjeeling Tea, Kanchipuram Silk Saree, Alphanso Mango, Nagpur Orange, Kolhapuri Chappal etc.,

### **Definitions**

Section 2 of the Act defines the terms used in the Act. The definition of some notable terms is given below:

#### **Geographical indication**

Geographical indication in relation to goods means an indication which identifies such goods as agricultural goods, natural goods or manufactured goods as originating, or manufactured in the territory of a country, or a region or locality in that territory, where a given quality, reputation or other characteristic of such goods is essentially attributable to its geographical origin and in case where such goods are manufactured goods one of the activities of either the production or of processing or preparation of the goods concerned takes place in such territory, region or locality, as the case may be.

It may be noted that any name which is not the name of a country, region or locality of that country shall also be considered as the geographical indication if it relates to a specific geographical area and is used upon or in relation to particular goods originating from that country, region or locality, as the case may be. [Section 2(e)]

#### **Goods**

Goods mean any agricultural, natural or manufactured goods or any goods of handicraft or of industry and includes food stuff. [Section 2(f)]

#### **Indication**

Indication includes any name, geographical or figurative representation or any combination of them conveying or suggesting the geographical origin of goods to which it applies. [Section 2(g)]

#### **Registration of geographical indication**

Section 8 of the Act provides that a geographical indication may be registered in respect of any or all of the goods, comprised in such class of goods as may be classified by a region or locality in that territory, as the case may be the Registrar and in respect of a definite territory of a country.

The Registrar may also classify the goods under in accordance with the International classification of goods for the purposes of registration of geographical indications and publish in the prescribed manner in an alphabetical index of classification of goods.

Any question arising as to the class within which any goods fall or the definite area in respect of which the geographical indication is to be registered or where any goods are not specified in the alphabetical index of goods published shall be determined by the Registrar whose decision in the matter shall be final.

## Prohibition of registration of certain geographical indications

**Section 9 of the Act prohibits registration of certain geographical indications. They are as follows :**

- (a) the use of which would be likely to deceive or cause confusion; or
- (b) the use of which would be contrary to any law for the time being in force; or
- (c) which comprises or contains scandalous or obscene matter; or
- (d) which comprises or contains any matter likely to hurt the religious susceptibilities of any class or section of the citizens of India; or
- (e) which would otherwise be disentitled to protection in a court; or
- (f) which are determined to be generic names or indications of goods and are, therefore, not or ceased to be protected in their country of origin, or which have fallen into disuse in that country; or
- (g) which, although literally true as to the territory, region or locality in which the goods originate, but falsely represent to the persons that the goods originate in another territory, region or locality, as the case may be, shall not be registered as a geographical indication.

It may be noted that "generic names or indications", in relation to goods, means the name of a goods which, although relates to the place or the region where the goods was originally produced or manufactured has lost its original meaning and has become the common name of such goods and serves as a designation for or indication of the kind, nature, type or other property or characteristic of the goods.

However, in determining whether the name has become generic, account shall be taken of all factors including the existing situation in the region or place in which the name originates and the area of consumption of the goods.

## Application for registration

Under section 11 any association of persons or producers or any organisation or authority established by or under any law for the time being in force representing the interest of the producers of the concerned goods, who are desirous of registering a geographical indication in relation to such goods shall apply in writing to the Registrar in such form and in such manner and accompanied by such fees as may be prescribed for the registration of the geographical indication.

The application shall contain -

- A single application may be a statement as to how the geographical indication serves to designate the goods as originating from the concerned territory of the country or region or locality in the country, as the case may be, in respect of specific quality, reputation or other characteristics of which are due exclusively or essentially to the geographical environment, with its inherent natural and human factors, and the production, processing or preparation of which takes place in such territory, region or locality, as the case may be;
- the class of goods to which the geographical indication shall apply;
- the geographical map of the territory of the country or region or locality in the country in which the goods originate or are being manufactured;

- the particulars regarding the appearance of the geographical indication as to whether it is comprised of the words or figurative elements or both;
- a statement containing such particulars of the producers of the concerned goods, if any, proposed to be initially registered with the registration of the geographical indication as may be prescribed; and
- such other prescribed particulars.

made for registration of a geographical indication for different classes of goods and fee payable therefore shall be in respect of each such class of goods. Every application shall be filed in the office of the Geographical Indications Registry within whose territorial limits, the territory of the country or the region or locality in the country to which the geographical indication relates is situated.

Every application shall be examined by the Registrar in such manner as may be prescribed. The Registrar may refuse the application or may accept it absolutely or subject to such amendments, modification, conditions or limitations, if any, as he thinks fit. In the case of refusal or conditional acceptance of application, the Registrar shall record in writing the grounds for such refusal or conditional acceptance and the materials used by him in arriving at his decision.

### **Registration**

Section 16 provides that on the registration of a geographical indication, the Registrar shall issue each to the applicant and the authorised users, if registered with the geographical indication, a certificate sealed with the seal of the Geographical Indications Registry.

It may be noted that where registration of a geographical indication is not completed within twelve months from the date of the application by reason of default on the part of the applicant, the Registrar may, after giving notice to the applicant in the prescribed manner treat the application as abandoned unless it is completed within the time specified in that behalf in the notice.

### **Duration of registration**

Section 18 of the Act deals with duration, renewal, removal and restoration of registration of Geographical Indication. The registration of a geographical indication shall be for a period of ten years, but may be renewed from time to time in accordance with the provisions of this section.

The registration of an authorised user shall be for a period of ten years or for the period till the date on which the registration of the geographical indication in respect of which the authorised user is registered expires, whichever is earlier.

The Registrar shall, on application made in the prescribed manner, by the registered proprietor or by the authorised user and within the prescribed period and subject to the payment of the prescribed fee, renew the registration of the geographical indication or authorised user, as the case may be, for a period of ten years from the date of expiration of the original registration or of the last renewal of registration, as the case may be.

### **Infringement of unregistered geographical indication**

As per section 20 of the Act a person shall not be entitled to institute any proceeding to prevent, or to recover damages for, the infringement of an unregistered geographical indication.

### **Infringement of registered geographical indications**

As per section 22 a registered geographical indication is infringed by a person who, not being an authorised

user thereof uses such geographical indication by any means in the designations or presentation of goods that indicates or suggests that such goods originate in a geographical area other than the true place of origin of such goods in a manner goods; or which misleads the persons as to the geographical origin of such goods; or uses any geographical indication in such manner which constitutes an act of unfair competition including passing off in respect of registered geographical indication.

It may be noted that "act of unfair competition" means any act of competition contrary to honest practices in industrial or commercial matters. The following acts shall be deemed to be acts of unfair competition, namely:

- all acts of such a nature as to create confusion by any means whatsoever with the establishment, the goods or the industrial or commercial activities, of a competitor;
- false allegations in the course of trade of such a nature as to discredit the establishment, the goods or the industrial or commercial activities, of a competitor;
- geographical indications, the use of which in the course of trade is liable to mislead the persons as to the nature, the manufacturing process, the characteristics, the suitability for their purpose, or the quantity, of the goods.

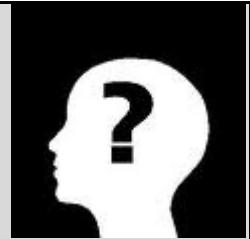
A registered geographical indication is infringed by a person who, not being an authorised user thereof uses another geographical indication to the goods which, although literally true as to the territory, region or locality in which the goods originate, falsely represents to the persons that the goods originate in the territory, region or locality in respect of which such registered geographical indication relates.

### **Assignment or transmission**

Section 24 of the Act prohibits assignment or transmission of geographical indication. It states that any right to a registered geographical indication shall not be the subject matter of assignment, transmission, licensing, pledge, mortgage or any such other agreement. However, on the death of an authorised user his right in a registered geographical indication shall devolve on his successor in title under the law for the time being in force.

#### ***Can a registered geographical indication be assigned, transmitted, etc?***

*No. A geographical indication is a public property belonging to the producers of the concerned goods. It shall not be the subject matter of assignment, transmission, licensing, pledge, mortgage or such other agreement. However, when an authorised user dies, his right devolves on his successor in title.*



### **Prohibition of registration of geographical indication as Trade mark**

Section 25 of the Act provides that the Registrar of Trade Marks shall, suo-motu or at the request of an interested party, refuse or invalidate the registration of a trade mark which contains or consists of a geographical indication with respect to the goods or class or classes of goods not originating in the territory of a country, or a region or locality in that territory which such geographical indication indicates, if use of such geographical indications in the trade mark for such goods, is of such a nature as to confuse or mislead the persons as to the true place of origin of such goods or class or classes of goods.

### **How a geographical indication is different from a trade mark?**

*A trade mark is a sign which is used in the course of trade and it distinguishes goods or services of one enterprise from those of other enterprises. Whereas a geographical indication is an indication used to identify goods having special characteristics originating from a definite geographical territory*



### **Special provisions relating to applications for registration from citizens of convention countries**

Section 84 empowers Central Government may by notification in the Official Gazette, declare such country or group of countries or union of countries or Inter-Governmental Organisations to be a convention country or convention countries for the purposes of the Act for the fulfillment of a treaty, convention or arrangement with any country or a country which is a member of a group of countries or union of countries or Inter-Governmental Organisations outside India which affords to citizens of India similar privileges as granted to its own citizens.

### **LESSON ROUND UP**

- Geographical Indications of Goods are that aspect of industrial property which refers to a country or to a place situated therein as being the country or place of origin of that product. Typically, such a name conveys an assurance of quality and distinctiveness which is essentially attributable to the fact of its origin in that defined geographical locality, region or country.
- Registration of GI confers legal protection to Geographical Indications in India; Prevents unauthorised use of a Registered Geographical Indication by others provides legal protection to Indian Geographical Indications which in turn boost exports; promotes economic prosperity of producers of goods produced in a geographical territory.
- The registration of a geographical indication shall be for a period of ten years, but may be renewed from time to time in accordance with the provisions of the Act.
- A person shall not be entitled to institute any proceeding to prevent, or to recover damages for, the infringement of an unregistered geographical indication.
- A geographical indication is a public property belonging to the producers of the concerned goods. It shall not be the subject matter of assignment, transmission, licensing, pledge, mortgage or such other agreement However, when an authorised user dies, his right devolves on his successor in title.

### **SELF TEST QUESTIONS**

1. What is a Geographical Indication?
2. What is the benefit of registration of geographical indications?
3. How long the registration of Geographical Indication is valid?
4. When is a registered Geographical Indication said to be infringed?
5. Can a registered geographical indication be assigned, transmitted, etc?

# INTELLECTUAL PROPERTY RIGHTS (DESIGNS ACT, 2000)

## Section VI

### LESSON OUTLINE

- Design
- Article
- Design which prohibited of registration
- Application for Registration
- Effect of registration of design
- Copyright on registration
- Piracy of registered design
- What is Piracy of a design

### LEARNING OBJECTIVES

Industrial designs refer to creative activity which result in the ornamental or formal appearance of a product and design right refers to a novel or original design that is accorded to the proprietor of a validly registered design. Industrial designs are an element of intellectual property.

Article 25 of the World Trade Organisation TRIPS Agreement, obliges Members to provide for the protection of independently created industrial designs that are new or original. A design which is not new or original; or which has been disclosed to the public anywhere; or which is not significantly distinguishable from known design or combination of known design; or which comprises or contains scandalous or obscene matter are prohibited for registration under the Design Act, 2000.

As a developing country, India has already amended its national legislation to provide for these minimal standards. India has also achieved a mature status in the field of industrial designs and in view of globalization of the economy, the Design law is aligned with the changed technical and commercial scenario and made to conform to international trends in design administration. Therefore, students should be well versed in Design Act, 2000.

The essential purpose of Design Act is to promote and protect the design element of industrial production. It is also intended to promote innovative activity in the field of industries.

## INTRODUCTION

The objective of the Designs Act, 2000 is to protect new or original designs so created to be applied or applicable to particular article to be manufactured by Industrial Process or means. Sometimes purchase of articles for use is influenced not only by their practical efficiency but also by their appearance. The important purpose of design Registration is to see that the artisan, creator, originator of a design having aesthetic look is not deprived of his bonafide reward by others applying it to their goods.

## DEFINITION

### Article

Under section 2(a) the Designs Act, 2000 article means any article of manufacture and any substance, artificial, or partly artificial and partly natural; and includes any part of an article capable of being made and sold separately.

### Design

As per section 2(d) Design means only the features of shape, configuration, pattern or ornament or composition of lines or colour or combination thereof applied to any article whether two dimensional or three dimensional or in both forms, by any industrial process or means, whether manual, mechanical or chemical, separate or combined, which in the finished article appeal to and are judged solely by the eye, but does not include any mode or principle or construction or anything which is in substance a mere mechanical device, and does not include any trade mark, as define in clause (v) of sub-section of Section 2 of the Trade and Merchandise Marks Act, 1958, property mark or artistic works as defined under Section 2(c) of the Copyright Act, 1957.

### Prohibition of registration of certain designs

A design which prohibited of registration under Design Act, 2000 are as follows:

- is not new or original; or
- has been disclosed to the public anywhere in India or in any other country by publication in tangible form or by use or in any other way prior to the filing date, or where applicable, the priority date of the application for registration; or
- is not significantly distinguishable from known designs or combination of known designs; or
- comprises or contains scandalous or obscene matter, shall not be registered.

### Application and Registration of design

Section 5 provides that the Controller may, on the application of any person claiming to be the proprietor of any new or original design not previously published in any country and which is not contrary to public order or morality register the design under the Act. Every application required to be in the prescribed manner and accompanied by the prescribed fee. A design when registered shall be registered as of the date of the application for registration.

As per section 7 the Controller shall, as soon as may be after the registration of a design, cause publication of the prescribed particulars of the design to be published in prescribed manner and the design be open to public inspection. Under section 9 of the Design Act, the Controller grant a certificate of registration to the proprietor of the design when it registered.

### Copyright on registration

Section 11 provides that when a design is registered, the registered proprietor of the design shall, subject to the provisions of this Act, have copyright in the design during ten years from the date of registration. However, before the expiration of the said ten years, application for the extension of the period of copyright is made to the Controller in the prescribed manner, the Controller shall, on payment of the prescribed fee, extend the period of copyright for a second period of five years from the expiration of the original period of ten years.

#### **What is the effect of registration of design?**

*The registration of a design confers upon the registered proprietor 'Copyright' in the design for the period of registration. 'Copyright' means the exclusive right to apply a design to the article belonging to the class in which it is registered.*



### Piracy of registered design

Under section 22 of the Act during the existence of copyright in any design it shall not be lawful for any person—

- for the purpose of sale to apply or cause to be applied to any article in any class of articles in which the design is registered, the design or any fraudulent or obvious imitation thereof, except with the licence or written consent of the registered proprietor, or to do anything with a view to enable the design to be so applied; or
- to import for the purposes of sale, without the consent of the registered proprietor, any article belonging to the class in which the design has been registered, and having applied to it the design or any fraudulent or obvious imitation thereof; or
- knowing that the design or any fraudulent or obvious imitation thereof has been applied to any article in any class of articles in which the design is registered without the consent of the registered proprietor, to publish or expose or cause to be published or exposed for sale that article.

If any person acts in contravention of the mentioned above, he shall be liable for every contravention.

#### **What is piracy of a Design?**

*Piracy of a design means the application of a design or its imitation to any article belonging to class of articles in which the design has been registered for the purpose of sale or importation of such articles without the written consent of the registered proprietor. Publishing such articles or exposing terms for sale with knowledge of the unauthorized application of the design to them also involves piracy of the design.*



## LESSON ROUND UP

- Design means only the features of shape, configuration, pattern or ornament or composition of lines or colour or combination thereof applied to any article whether two dimensional or three dimensional or in both forms, by any industrial process or means, whether manual, mechanical or chemical, separate or combined, which in the finished article appeal to and are judged solely by the eye, but does not include any mode or principle or construction or any thing which is in substance a mere mechanical device, and does not include any trade mark.
  - The duration of the registration of a design is initially ten years from the date of registration, but in cases where claim to priority has been allowed the duration is ten years from the priority date. This initial period of registration may be extended by further period of 5 years on an application to the Controller before the expiry of the said initial period.
  - The registration of a design may be cancelled at any time after the registration of design on a petition for to the Controller of Designs on the grounds of that the design has been previously registered in India or it has been published in India or elsewhere prior to date of registration or the design is not new or original or Design is not registrable or is not a design under Clause (d) of Section 2 of the Act.

## SELF TEST QUESTION

1. What is meant by 'Design' under the Designs Act, 2000 ?
  2. What is the object of registration of Designs?
  3. What is the effect of registration of design?
  4. What is piracy of a Design?
  5. What is the penalty for the piracy of a registered Design?

# Lesson 5

## LAW RELATING TO ARBITRATION AND CONCILIATION

### LESSON OUTLINE

- Introduction to UNCITRAL Model Law
- Law of Arbitration in India
- Arbitration
- Types of Arbitration
- Arbitration Agreement
- Appointment of Arbitrators
- Arbitral procedure
- Arbitral Tribunal
- Appointment of experts by Arbitral Tribunal
- Arbitral Award
- Appeals
- Enforcement of Foreign Award
- Arbitration and Conciliation
- Conciliation
- Arbitral Proceedings
- Appointment of Conciliator
- Confidentiality
- Role of Conciliator
- International Commercial Arbitration
- Alternate Disputes Resolution

### LEARNING OBJECTIVES

Arbitration is the means by which parties to a dispute get the same settled through the intervention of a third person (or more persons) but without recourse to a Court of Law. The settlement of dispute is arrived by the judgment of the third person (or more persons) who are called Arbitrators. The parties repose confidence in the judgement of the arbitrator and show their willingness to abide by his decision.

The essence of arbitration is thus based upon the principle of keeping away the dispute from the ordinary Courts enabling the parties to substitute by a domestic tribunal. It is, therefore, a reference of the matter of disputes to the decision of one or more persons between the disputing parties.

United Nations Commission on International Trade Law (UNCITRAL) has adopted the UNCITRAL Model Law on International Commercial Arbitration in 1985 and the General Assembly of the United Nations has recommended that all countries give due consideration to the said Model Law, in view of the desirability of uniformity of the law of arbitral procedures and the specific needs of international commercial arbitration practice. The Arbitration and Conciliation Act, 1996 is based on United Nations Commission on International Trade Law (UNCITRAL) Model Law on International Commercial Arbitration.

Therefore, students should be well versed in this subject so as to understand Arbitration, Conciliation, International Commercial Arbitration and Alternate Disputes Resolution.

The Arbitration and Conciliation Act, 1996 is an Act to consolidate and amend the law relating to domestic arbitration, international commercial arbitration and enforcement of foreign arbitral awards as also to define the law relating to conciliation and for matters connected therewith or incidental thereto.

## INTRODUCTION

The history of the law of arbitration in India commences with Act VIII of 1859 which codified the procedure of Civil Courts. Sections 312 to 325 of Act VIII of 1859 dealt with arbitration between the parties to a suit while Sections 326 and 327 dealt with arbitration without the intervention of the Court. These provisions were in operation when the Indian Contract Act, 1872, came into force which permitted settlement of disputes by arbitration under Section 28 thereof. Act VIII of 1859 was followed by later codes relating to Civil Procedure, namely, Act X of 1877 and Act XIV of 1882 but not much change was brought about by the law relating to arbitration proceedings. It was in the year 1899 that an Indian Act entitled the Arbitration Act of 1899 came to be passed. It was based on the model of the English Act of 1899. The 1899 Act applied to cases where if the subject matter submitted to the arbitration was the subject of a suit, the suit could whether with leave or otherwise, be instituted in a Presidency town. Then came the Code of Civil Procedure of 1908. Schedule II to the said Code contained the provisions relating to the law of arbitration which extended to the other parts of British India.

The Civil Justice Committee in 1925 recommended several changes in the arbitration law. On the basis of the recommendations by the Civil Justice Committee, the Indian Legislature passed the Act, i.e., the Arbitration Act of 1940. This Act as its preamble indicates is a consolidating and amending Act and is an exhaustive code insofar as the law relating to arbitration is concerned. An arbitration may be without the intervention of a Court or with the intervention of a Court where there is no suit pending or it may be an arbitration in a suit.

With the passage of time the 1940 Act became outmoded, and need was expressed by the Law Commission of India and various representative bodies of trade and industry for its amendment so as to be more responsive to the contemporary requirements, and to render Indian economic reforms more effective. Besides, arbitration, other mechanisms of settlement of disputes such as mediation or conciliation should have legal recognition and the settlement agreement reached between the parties as a result of such mechanism should have the same status and effect as an arbitral award on agreed terms.

## Arbitration and Conciliation Act, 1996

With a view to consolidate and amend the law relating to domestic arbitration, international commercial arbitration, enforcement of foreign arbitral awards and also to provide for a law relating to conciliation and related matters, a new law called Arbitration and Conciliation Act, 1996 has been passed. The new Law is based on United Nations Commission on International Trade Law (UNCITRAL), model law on International Commercial Arbitration.

The Arbitration and Conciliation Act, 1996 aims at streamlining the process of arbitration and facilitating conciliation in business matters. The Act recognizes the autonomy of parties in the conduct of arbitral proceedings by the arbitral tribunal and abolishes the scope of judicial review of the award and minimizes the supervisory role of Courts. A significant feature of the Act is the appointment of arbitrators by the Chief Justice of India or Chief Justice of High Court. The Chief Justice may either appoint the arbitrator himself or nominate a person or Institution to nominate the arbitrator. The autonomy of the arbitral tribunal has further been strengthened by empowering them to decide on jurisdiction and to consider objections regarding the existence or validity of the arbitration agreement.

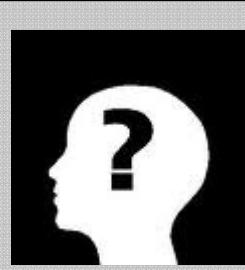
The Act has been divided into four Parts and contains three Schedules. Part one deals with Arbitration (Sections 2 to 43); Part two deals with enforcement of certain Foreign Awards (Sections 44 to 60); Part three deals with conciliation (Sections 61 to 81); and Part four contains supplementary provisions (Sections 82 to

86). Similarly schedule one contains provisions relating to convention on the Recognition and Enforcement of Foreign Arbitral Awards; Schedule two deals with Protocol on Arbitration Clauses and Schedule three contains provisions relating to Execution of Foreign Arbitral Awards.

### **Test your knowledge**

**State whether the following statement is “True” or “False”**

With the passage of time the 1940 Act became outmoded, and need was expressed by the Law Commission of India and various representative bodies of trade and industry for its amendment so as to be more responsive to the contemporary requirements, and to render Indian economic reforms more effective.



- True
- False

**Correct answer: True**

### **Arbitration**

Section 2(1) (a) of the Act, defines the term “arbitration” as to mean any arbitration whether or not administered by a permanent arbitral institution.

### **Arbitrator**

The term “arbitrator” is not defined in the Arbitration and Conciliation Act. But “arbitrator” is a person who is appointed to determine differences and disputes between two or more parties by their mutual consent. It is not enough that the parties appoint an arbitrator. The person who is so appointed must also give his consent to act as an arbitrator. His appointment is not complete till he has accepted the reference. The arbitrator must be absolutely disinterested and impartial. He is an extra-judicial tribunal whose decision is binding on the parties.

Any interest of the arbitrator either in one of the parties or in the subject-matter of reference unknown to either of the parties or all the parties, as the case may be, is a disqualification for the arbitrator. Such disqualification applies only in the case of a concealed interest. If the arbitrator has an interest in the subject-matter of reference well-known to the parties before they sign the submission, the award is good notwithstanding his own interest. Every disclosure which might in the least affect the minds of those who are proposing to submit their disputes to the arbitration of any particular individual as regards his selection and fitness for the post ought to be made so that each party may have an opportunity of considering whether the reference to arbitration to that particular individual should or should not be made.

The parties may appoint whomsoever they please to arbitrate on their dispute. Usually the parties themselves appoint the arbitrator or arbitrators. In certain cases, the Court can appoint an arbitrator or umpire. The parties to an arbitration agreement may agree that any reference thereunder shall be referred to an arbitrator or arbitrators to be appointed by a person designated in the agreement either by name or as the holder for the time being of any office or appointment.

### **Arbitral Award**



As per Section 2(1)(c), "arbitral award" includes an interim award. The definition does not give much details of the ingredients of an arbitral award. However, taking into account other provisions of the Act, the following features are noticed:

1. An arbitration agreement is required to be in writing. Similarly, a reference to arbitration and award is also required to be made in writing. The arbitral award is required to be made on stamp paper of prescribed value (as applicable at the place of making the award) and in writing. An oral decision is not an award under the law.
2. The award is to be signed by the members of the arbitral tribunal. However, the signature of majority of the members of the tribunal is sufficient if the reason for any omitted signature is stated.
3. The making of an award is a rational process which is accentuated by recording the reasons. The award should contain reasons. However, there are two exceptions where an award without reasons is valid i.e.
  - (a) Where the arbitration agreement expressly provides that no reasons are to be given, or
  - (b) Where the award has been made under Section 30 of the Act i.e. where the parties settled the dispute and the arbitral tribunal has recorded the settlement in the form of an arbitral award on agreed terms.

The formulation of reasons is a powerful discipline and it may lead the arbitrator to change his initial view on the matter. Recording of reasons involves, analysis of the dispute to reach a logical conclusion. Award can be divided into four parts i.e. general, findings of fact, submissions of the parties and conclusions of the tribunal. The tribunal should explain its view of the evidence and reasons of its conclusions. The preamble of the award may contain reference to the arbitration agreement, constitution of the tribunal, procedure adopted by the tribunal etc. and the second part of the award may contain points at issue, argument for the claimant, argument for the respondent and findings of the tribunal. The points at issue may be divided into two heads i.e. issue of fact and issue of law.

4. The award should be dated i.e. the date of making of the award should be mentioned in the award.
5. Place of arbitration is important for the determination of rules applicable to substance of dispute, and recourse against the award. The arbitral tribunal is under obligation to state the place of arbitration as determined in accordance with Section 20. Place of arbitration refers to the jurisdiction of the Court of a particular city or State.
6. The arbitral tribunal may include in the sum for which award is made, interest upto the date of award and also a direction regarding future interest.
7. The award may also include decisions and directions of the arbitrator regarding the cost of the arbitration.
8. After the award is made, a signed copy should be delivered to each party for appropriate action like implementation or recourse against arbitral award.

### **Arbitral Tribunal**

“Arbitral tribunal” means a sole arbitrator or a panel of arbitrators.[Section 2(1)(d)].

### **Court**

“Court” means the Principal Civil Court of original jurisdiction in a district and includes the High Court in exercise of its ordinary original civil jurisdiction, having jurisdiction to decide the questions forming the subject matter of the arbitration if the same had been the subject matter of a suit, but does not include any Civil Court of a grade inferior to such principal Civil Court or any Court of Small Causes.[Section 2(1)(e)]

## International Commercial Arbitration

“International commercial arbitration” means an arbitration relating to disputes arising out of legal relationships, whether contractual or not, considered as commercial under law in force in India and where at least one of the parties is:

- (i) an individual who is a national of, or habitual resident in, any country other than India; or
- (ii) a body corporate which is incorporated in any country other than India; or
- (iii) a company or an association or a body of individuals whose central management and control is exercised in any country other than India; or
- (iv) the Government of a foreign country. [Section 2(1)(f)]

## Legal Representative

The definition of “legal representative” given under Section 2(1)(g) has been taken verbatim from the definition in Section 2(11) of the Code of Civil Procedure.

The following are the persons who are legal representatives:

- (a) A person who in law represents the estate of a deceased person.
- (b) A person who intermeddles with the estate of the deceased.
- (c) A person on whom the estate of a deceased person devolves on the death of the party acting in a representative's capacity.

The following persons are generally included in the list of legal representatives.

- (i) Executors and administrators properly appointed.
- (ii) Person who has taken on himself duties and responsibilities which belong to the executor or administrator though only in respect of a part of the estate.
- (iii) Heirs-at-law whether they take succession or by survivorship.
- (iv) Revisioners when the action has been brought by or against the widow representing her husband's estate.
- (v) Universal legatee.

The following are the illustrations of those who do not come within the meaning of legal representative, so far as the Act is concerned:

- (i) An assignee from a deceased zamindar or to whom the holding reverts on the death of a tenant.
- (ii) A trespasser or a person who claims adversely the estate of the deceased.
- (iii) A new trustee appointed or elected on the death of the deceased trustee.

## Arbitration Agreement



“Arbitration agreement” means an agreement referred to in Section 7 [Section 2(1)(b)]. Under Section 7, the “Arbitration agreement” has been defined to mean an agreement by parties to submit the arbitration or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship whether contractual or not. Sub-section (2) says that an arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

Sub-section (3) specifically states that an arbitration agreement shall be in writing. Sub-section (4) spells out that an arbitration agreement is in writing if it is contained in

- (a) a document signed by the parties, or
- (b) an exchange of letters, telex, telegrams or other means of telecommunication, which provide a record of the agreement, or
- (c) an exchange of statements of claim and defence in which the existence of the agreement is alleged by one party and not denied by the other.



Thus, arbitration agreement stands on the same footing as any other agreement. It is binding upon the parties unless it is influenced by fraud or coercion or undue influence, etc. As per Section 7, one of the essential ingredients of an arbitration agreement is that such an agreement should be in writing. An oral arbitration agreement is not recognised as an arbitration agreement according to this Section.

Sub-section (5) states that the reference in a contract to a document containing an arbitration clause constitutes an arbitration agreement if the contract is in writing and the reference is such as to make that arbitration clause part of the contract.

Sub-section (3) only requires that an agreement by the parties should be in writing. It is not necessary that the words arbitration, arbitrator or arbitration agreement should appear in the arbitration clause so long as the parties have valid agreement to allow the matter of dispute to be decided by persons of their own choice.

Under the present law, certain disputes such as matrimonial disputes, criminal prosecutions, questions relating to guardianship about the validity of a will, etc. are treated as not suitable for arbitration. Subject to this qualification Section 7(1) of the Act makes it permissible to enter into an arbitration agreement "in respect of a defined legal relationship, whether contractual or not". It expressly recognizes that the arbitrator will have such a power to commence or continue the arbitral proceedings though the objecting party can obtain a ruling of the court at the appropriate time.

**The Supreme Court in *Hindustan Petroleum Corporation Ltd. v. M/s Pink City Midway Petroleum*, AIR 2003 SC 2881 has held that the jurisdiction of Civil Court is barred after an application under Section 8 of the Act is made for arbitration.**

In *Mahesh Kumar v. Rajasthan State Road Corporation*, AIR 2006 Raj 56, the Rajasthan High Court has held that mere existence of arbitration clause in agreement does not bar jurisdiction of Civil Court automatically. The objection of a party to the jurisdiction of the arbitrator must be raised not later than the submission of its first statement of defence on the substance of the dispute [Section 8(1) and 8(3)].

### **Test your knowledge**

#### **Choose the correct answer**

Which of the following is not a feature of an arbitral agreement?

- (a) Oral
- (b) Mention of place
- (b) Bearing a date
- (c) Written

**Correct answer: (a)**

## APPOINTMENT OF ARBITRATORS

Section 11 of the Act deals with appointment of arbitrators. According to this Section, parties can agree to any procedure for appointment of arbitrators. But provisions have been made to ensure timely appointments as under:

- (a) The parties may agree to a procedure of appointment of arbitrators. Otherwise the following procedure shall apply :
  - (i) Arbitrator could be of any nationality. [Section 11(1)]
  - (ii) In case of an arbitration with three arbitrators, each party shall appoint its own arbitrator, and the two appointed arbitrators shall appoint a third arbitrator, who shall be the presiding arbitrator [Section 11(3)].
  - (iii) If, within 30 days, the parties fail to appoint their arbitrators, or the two appointed arbitrators fail to agree on the third arbitrator, the arbitrator shall be appointed by the Chief Justice or any person or institution designated by him at the request of a party. [Section 11(4)]
  - (iv) Similar procedure is also applicable for appointment of a sole arbitrator. If parties fail to agree on the appointment of a sole arbitrator within 30 days, the appointment shall be done by the Chief Justice or a person/institution designated by him.
- (b) Similar procedure also applies, when the procedure agreed by the parties is not acted upon in time. [Section 11(6)]
- (c) Decision on appointment of arbitrators by the Chief Justice or persons/ institution designated by him, is final [Section 11(7)].
- (d) Chief Justice or the persons/Institution designated by him would have due regard to qualifications of arbitrators agreed between the parties, and considerations likely to secure an independent and impartial arbitrator. [Section 11(8)]
- (e) In case of appointment of a sole or third arbitrator in an international commercial arbitration, the Chief Justice of India or a person/Institution designed by him, may appoint a person of a nationality, other than that of the parties, where the parties are of different nationalities. [Section 11(9)]
- (f) The Chief Justice can make any Scheme, he considers appropriate for appointment of arbitrators under Sub-section (4), (5) or (6).

In a case original agreement was given a go-by and a new procedure for appointment of arbitrator was agreed upon by the parties. However, respondent failed to appoint an arbitrator according to new method also. Calcutta High Court held that the other party can very well approach the court for appointment of an arbitrator under Section 11(5) of the Arbitration and Conciliation Act, 1996 (*Manoranjan Mandal and others v. Union of India and others*, AIR 1999 Cal. 117).

It has been held by the Supreme Court in *M/s S.B. P. & Co. v. M/s Patel Engg. Ltd.*, AIR 2006 SC 450 that the power exercised by the Chief Justice of the High Court or the Chief Justice of India under Section 11(6) of the Act is not an administrative power. It is a Judicial power. The power under Section 11(6) of the Act in its entirety, could be delegated, by the Chief Justice of the High Court only to another Judge of that Court and by the Chief Justice of India to another Judge of the Supreme Court. Designation of a District Judge as the authority under Section 11(6) of the Act by the Chief Justice of the High Court is not warranted on the Scheme of the Act.

The mode of appointment of arbitrator may not always work very smoothly in actual practice. But this may

provide further opportunities for the organisations like Indian Council of Arbitration, International Centre for Alternate Dispute Resolution etc. Under the Act, an arbitrator before accepting his appointment is required to disclose to the parties in writing about such matters which may create doubts about his impartiality or independence. Where such doubts exist, his appointment can be challenged. Similarly, where the arbitrator does not possess the required or the agreed qualification for the appointment, his appointment can be challenged as per Sections 12 and 13 of the Act.

### **Number of arbitrators**

Section 10 of the Act provides that, the parties are free to determine the number of arbitrators, provided that such number shall not be an even number. If they fail to determine the number of arbitrators, the arbitral tribunal shall consist of a sole arbitrator.

There is nothing in Section 7 to indicate the requirement of the number of arbitrators as a part of the arbitration agreement. Thus, the validity of an arbitration agreement would not depend on the number of arbitrators specified therein. The number of arbitrators is dealt with separately in Section 10 which is a part of the machinery provision for the working of the arbitration agreement. It is therefore, clear that an arbitration agreement specifying an even number of arbitrators could not be a ground to render the arbitration agreement invalid under the Act (*MMTC Ltd. v. Sterlite Industries (India) Ltd.*, (1996) 8 Scale 305).

### **Grounds for challenge**

The appointment of arbitrators made under Section 11 of the Act, can be challenged on the grounds as specified in Section 12 of the Act. For that purpose, Section 13 contains the procedure. According to Section 12 of the Act when a person is approached in connection with his possible appointment as an arbitrator, he shall disclose in writing any circumstances likely to give rise to justifiable doubts as to his independence or impartiality. Some examples of such circumstances may be blood relationship or pecuniary relationship with either party to the dispute. Moreover, an arbitrator, from the time of his appointment and throughout the arbitral proceedings, shall without delay, disclose to the parties in writing any circumstances referred to above unless they have already been informed of them by him. An arbitrator may be challenged by a party only if (1) circumstances exist that give rise to justifiable doubts as to his independence or impartiality, or (2) he does not possess the qualifications agreed to by the parties. Sub-section 4 of Section 12 makes it clear that a challenge is also permitted, if a party becomes aware of these grounds after an appointment is made.

### **Challenge procedure**

Section 13 of the Act contains detailed provisions regarding challenge procedure. Sub-section (1) provides that subject to provisions of Sub-section (4), the parties are free to agree on a procedure for challenging an arbitrator. Sub-Section (4) states that if a challenge under any procedure agreed upon by the parties or under the procedure under Sub-section (2) is not successful, the arbitral tribunal shall continue the arbitral proceedings and make an arbitral award. But at that stage, the challenging party has the right to make an application in the Court to set aside the award in accordance with Section 34 of the Act.

Sub-section (2) provides that failing any agreement referred to in Sub-section (1) of Section 13, a party who intends to challenge an arbitrator shall, within 15 days after becoming aware of the constitution of the arbitral tribunal or after becoming aware of any circumstances referred to in Sub-section (3) of Section 12, send a written statement of the reasons for the challenge to the arbitral tribunal. The tribunal shall decide on the challenge unless the arbitrator challenged under sub-section (2) withdraws from his office or the other party agrees to the challenge. It is also provided that where an award is set aside on an application made under Sub-section (5) of Section 13 of the Act, the Court may decide as to whether the arbitrator who is challenged is entitled to any fees.

### Failure or impossibility to act as an arbitrator

As per Section 14(1), the mandate of an arbitrator shall terminate, if he becomes *de jure* or *de facto* unable to perform his functions, or fails to act without undue delay due to some other reasons. Mandate is also terminated, if he withdraws from his office, or the parties agree to the termination of his mandate.

Further, if there is a controversy about an arbitrator's inability to function or occurrence of undue delay, a party may seek intervention of the Court under Section 14(2).

However, withdrawal by arbitrator on his own or by agreement between the parties does not constitute acceptance of the grounds of challenge.

It is considered that the procedure for challenge to the appointment of an arbitrator need not be a matter of agreement by parties. The procedure in Section 13 should apply in all cases.

### Substitution of Arbitrator

- (1) In addition to the circumstances referred to in Section 13 or Section 14, the mandate of an arbitrator shall terminate—
  - (a) where he withdraws from office for any reasons; or
  - (b) by or pursuant to agreement of the parties.
- (2) Where the mandate of an arbitrator terminates, a substitute arbitrator shall be appointed according to the rules that were applicable to such appointment being replaced.
- (3) Unless otherwise agreed by the parties, where an arbitrator is replaced under Sub-section (2), any hearings previously held may be repeated at the discretion of the arbitral tribunal.
- (4) Unless otherwise agreed by the parties, an order or ruling of the arbitral tribunal made prior to the replacement of an arbitrator under this Section shall not be invalid solely because there has been a change in the composition of the arbitral tribunal [Section 15].

## ARBITRAL PROCEEDINGS

### Place and commencement of arbitration

As per Section 20 of the Act, the parties are free to agree on the place of arbitration and if they fail to reach an agreement, the place of arbitration is determined by the arbitral tribunal, having regard to the circumstances of the case, including the convenience of the parties. Section 20(3) introduces an option by providing that the arbitrator/tribunal may, unless otherwise agreed by the parties, may meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of documents, goods or other property. Section 31(4) makes it mandatory for the arbitral tribunal to state in the arbitral award the date and the place of arbitration as determined in accordance with Section 20 and the award is then deemed to have been made at that place. Part-II of the Act deals with foreign awards and is applicable to those awards made outside the territory of India. Hence, place of arbitration has far reaching effect in terms of law applicable to arbitration and also enforcement of the arbitral award in international commercial arbitration. Place of arbitration in an arbitration other than international commercial arbitration i.e. in domestic arbitration, does not pose any problem. Parties may agree on the place of arbitration anywhere in India. But in international commercial arbitration, place of arbitration has legal implications in terms of law applicable to arbitration. In domestic arbitration, the arbitral tribunal has to decide the dispute in accordance with the Indian law, but in international commercial arbitration, parties have been given freedom to designate law applicable to the substance of the dispute and the arbitral tribunal may apply the rules of law agreed by the parties.

Section 21 stating that the arbitral proceedings commence on the date on which a request for that dispute to be referred to arbitration is received by the respondent. No time limit has been prescribed under the Act. However, where the arbitrator is guilty of undue delay, his proceedings can be put to a stop as per Section 14(1) of the Act.

### **Language of arbitration**

Section 22 gives freedom to parties to agree upon the language or languages to be used in the arbitral proceedings. The arbitral tribunal, subject to agreement of parties, has power to determine the language or languages to be used in the arbitral proceedings. Generally, the language of arbitration is English. It being the international language, the same is agreed in most of the arbitrations by the parties and the arbitral tribunal. The arbitral tribunal may ask for translation of documentary evidence into the or languages agreed upon by the parties or determined by the arbitral tribunal.

### **Test your knowledge**

#### **Choose the correct answer**

Which of the following circumstances lead to a termination of the mandate of an arbitrator?

- (a) If he becomes unable to perform his functions
- (b) If the parties agree to the termination of his mandate
- (c) If he withdraws from his office
- (d) If he performs all duties in an appropriate and timely manner

**Correct Answer: a, b and c**

### **Arbitration procedure**

Sections 23 to 27 stipulate the procedure to be followed in arbitration proceedings. It gives a comprehensive guidance regarding the procedure such as filing of a claim, submission of difference, amendment of claim/defences etc. Sections 23 and 24 of the Act set out the stages of arbitration proceedings in an orderly manner. Section 23 of the Act provides that:

- (1) Within the period of time agreed upon by the parties as determined by the arbitral tribunal, the claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought, and the respondent shall state his defence in respect of these particulars, unless the parties have otherwise agreed as to the required elements of those statements.
- (2) The parties may submit with their statements all documents they consider to be relevant or may add a reference to the documents or other evidence they will submit.
- (3) Unless otherwise agreed by the parties, either party may amend or supplement his claim or defence during the course of the arbitral proceedings, unless the arbitral tribunal considers it inappropriate to allow the amendment or supplement having regard to the delay in making it.

Section 18 lays down two obligations on the arbitral tribunal i.e. to treat the party with equality and to give full opportunity to each party to present his case. Section 18 which is one of the most significant Sections, constitutes a fundamental principle which is applicable to entire proceedings. The principle of equality and full opportunity to present the case should be observed by the parties also, when laying down any rules of procedure. An agreed procedure which violates the fundamental principle of equality and granting of an opportunity of being heard, is null and void and an award passed in violation of this principle can be set

aside. Section 34(2) provides that an award may be set aside if the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of the law from which parties cannot derogate, or, failing such agreement, was not in accordance with law. Hence, an agreement cannot be in conflict with a mandatory provision of the law. If procedure agreed by the parties violates the fundamental principles, it cannot be enforced by the arbitral tribunal. The principle enshrined in Section 18 should be observed during the entire arbitral proceedings. The principle does not entitle a party to adopt delaying tactics to obstruct the proceedings. The general principle is, however, subject to other provisions contained in Sections 23, 24 and 25, wherein the right can be curtailed or limited by the parties or by the arbitral tribunal in certain cases. The parties may agree that arbitration be conducted on the basis of documents only under Section 23(1). Hence, Section 18 is influenced by Sections 23, 24 and 25 and at the same time Section 18 must also influence these Sections. The arbitral tribunal has to maintain a balance for smooth conduct of the proceedings and has to make the parties feel that the arbitral tribunal is giving them full opportunity to present documents, witnesses and arguments. The parties are entitled to legal representation by the person of their choice and if disallowed, it could be violation of the principle of giving a full opportunity of presenting the case.

Section 24 of the Act deals with hearings and written proceedings. There is no restriction upon the parties to agree for holding oral hearings for presentation of evidence and for oral arguments or, alternatively, for conducting the proceedings on the basis of documents. Otherwise the arbitral tribunal shall decide whether to hold oral hearing for the presentation of evidence or for oral argument, or whether the proceedings shall be conducted on the basis of documents and other materials, provided that arbitral tribunal shall hold hearings, at an appropriate stage of the proceedings, on a request by a party, unless the parties agreed that no oral hearings shall be held.

Sub-section 2 of Section 24 requires that the parties shall be given sufficient advance notice of any hearing and of any meeting of the arbitral tribunal for the purpose of inspection of documents, goods or other property. Further Section 24 provides that all documents/statements/other information received from one party must be communicated to the other parties.

### **Statements of claims and defence**

Within the period of time agreed upon by the parties or determined by the tribunal, the claimant has to state the facts in supporting his claim, the points at issue and the relief or remedy sought. Similarly, the respondent shall also state his defence in respect of these particulars.

### **Submission of documents**

Sub-section (2) of Section 23 provides that the parties may submit with their statements all documents they consider to be relevant or may add a reference to the documents or other evidence which they will submit later on.

### **Amendments**

Parties may amend or supplement these statements during the proceedings, unless:

- (1) Parties have agreed otherwise, or
- (2) Arbitral tribunal considers it inappropriate to allow the amendment or supplement, due to delay in making it.

### **Determination of rules of arbitral procedure**

According to Section 19(1) the arbitral tribunal is neither bound by the Code of Civil Procedure 1908, nor by

the Indian Evidence Act, 1872. The Code of Civil Procedure is the Code of Civil Judicature and provides rules relating to suits, place of suing, summons and discovery, judgement and decree, interest, costs etc. The Evidence Act makes the law relating to evidence and applies to all judicial proceedings in or before the Court but not to proceedings before any arbitral tribunal. The arbitral tribunal is not bound to follow the procedure as followed by a Court. However, the arbitral tribunal is to observe fundamental principles envisaged under the Code of Civil Procedure and the Evidence Act. The procedure adopted by the arbitral tribunal should be according to the principles of natural justice.

Section 19(2) provides that subject to provisions of the Part I, the parties are free to agree on a procedure to be followed by the arbitral tribunal in conducting its proceedings. Rules of permanent arbitral Institutions usually deal with procedural matters in detail and are generally well tested in practice and are revised after consultation with experts to take into account fresh development in the law and practice of arbitration. Parties generally incorporate arbitration rules of a particular institution by reference to the same in the agreement. The arbitral tribunal does not have any discretion where any such rule has been provided for in the agreement itself.

The arbitral tribunal may conduct the proceedings in the manner it considers appropriate, but such power is subject to two exceptions mentioned below:

- (1) The arbitral tribunal cannot conduct the proceedings in a manner which is in violation of the mandatory provisions of the law.
- (2) The arbitral tribunal cannot conduct proceedings in a manner which is in violation of the procedure agreed by the parties, if any. Where parties have agreed on the procedure to be followed by the arbitral tribunal in conducting its proceedings the arbitral is bound to follow that procedure.

There is no mandatory provision in the Act as to how to determine the admissibility, relevance, materiality and weight of evidence. The parties may agree on the rules relating to this important aspect of the matter. However, if there are no agreed rules by the parties, the arbitral tribunal has power to determine the admissibility, relevance, materiality and weight of any evidence and make decision in the manner it considers appropriate. Section 19 recognizes the freedom of the parties to lay down as to how to conduct the proceedings subject to agreement of the parties. Freedom to lay down rules of procedure is, subject to following restrictions (mandatory provisions) laid down by law:

- (1) Submission of a statement of a claim and defence under Section 23.
- (2) The parties should be given sufficient advance notice of any hearing and of any meeting of the arbitral tribunal for purposes of inspection of documents, goods or other property under Section 24(2).
- (3) All statements, documents or other information supplied to or applications made to the arbitral tribunal by one party should be communicated to the other party and any expert report or evidentiary document on which arbitral tribunal may rely in making its decision should be communicated to the parties, as per Section 24(3).
- (4) The arbitral tribunal, or a party with the approval of the arbitral tribunal, is allowed to request the Court in taking evidence under Section 27.
- (5) An award in agreed terms must state that it is an award and should be in accordance with Section 30.
- (6) An arbitral award must be in writing and signed by the majority of all the members of the arbitral tribunal as per Section 31(1).
- (7) The arbitral award must state its date and place of arbitration under Section 31(4).

- (8) A copy of the award duly signed by the arbitral tribunal should be delivered to each party under Section 31(5).
- (9) The arbitral proceedings are terminated by the final arbitral award or by an order of the arbitral award under Section 32(2).
- (10) The arbitral tribunal has power to correct any computation errors, any clerical or typographical errors or any other errors of a similar nature and to give interpretation of a specific point or part of the award under Section 33.

Judges are bound by the Code of Civil Procedure and also by the Rules of the Court while conducting proceedings in the Court. There is no corresponding arbitration procedure and rules. Permanent arbitral institutions have their own sets of arbitration rules, but those rules do not regulate the procedure in detail. The arbitral tribunal is master of the procedure of arbitration, subject, of course, to restrictions imposed by law, agreement of parties and natural matter for a quick and cheap resolution of disputes.

### **Power to terminate/continue the proceedings**

Section 25 of the Act provides that subject to agreement between the parties, where, without showing sufficient cause, the claimant fails to communicate his statement of claim within the agreed period, the arbitration proceedings shall be terminated by the arbitrator. Similarly, where the respondent fails to communicate his statement of defence within the predetermined period, the arbitrator shall continue the proceedings without treating such failure, in itself, as an admission of the claimant's allegations. Further, when a party fails to appear at an oral hearing or to produce documentary evidence in support of its averment, the arbitrator can proceed and pronounce the award on the basis of evidence available before it. Thus, the general principles of ex parte proceedings will apply to arbitration proceedings also.

### **Appointment of experts by Arbitral Tribunal**

Section 26(1) of the Act, provides for appointment of experts subject to agreement between the parties. Clause (b) of Sub-section (1) of the Section obligates the parties to provide the expert access to necessary information and documents.

The provisions stipulated under Section 26(3) imposes a duty on the expert to make available to the parties on their request the various documents etc. on which the expert has based his report.

### **Decision by majority**

Section 29 of the Act provides for decision by majority where there is more than one arbitrator.

### **Court assistance**

Provisions are also made under the Act relating to Court assistance in taking evidence. Section 27 of the Act provides that the arbitral tribunal, or a party with the approval of the arbitral tribunal, may apply to the court for assistance in taking evidence. For this purpose the application must specify the names and addresses of the parties and the arbitrators, general nature of the claim and the relief sought and the evidence to be obtained particularly (1) the name and address of any person to be heard as witness or expert witness and a statement of the subject matter of the testimony required; (2) the description of any document to be produced or property to be inspected. According to Sub-section (3), the Court may execute the request by ordering that the evidence be provided directly to the arbitral tribunal. Parties shall be subject to the same disadvantage, punishments and penalties by order of the Court, as they would incur for the like offences in suits tried by the Court when persons fail to attend, or make a default, or refuse to give evidence or guilty of contempt of the tribunal during the conduct of the proceedings.

## **Jurisdiction of Arbitral Tribunals**

The arbitral tribunal is empowered to rule its own jurisdiction including any objections in relation to existence and validity of the arbitration agreement. Section 16 of the Act relates to competence of arbitral tribunal to rule on its jurisdiction, including ruling on any objections with respect to the existence or validity of the arbitration agreement. For this purpose:

- (1) an arbitration clause which forms part of a contract shall be treated as an agreement independent of other terms of the contract; and
- (2) a decision by the arbitral tribunal that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause.

Section 16 also contains in its ambit pleas of non-jurisdiction or excess of authority. Sub-section (2) of Section 16 provides that a plea can be raised not later than the submission of the statement of defence where the arbitral tribunal does not have jurisdiction. It is further provided that a party shall not be precluded from raising such a plea merely because he has appointment or participated in the appointment of an arbitrator. Likewise, Sub-section (3) of Section 16 provides that a plea that the arbitral tribunal is exceeding the scope of its authority, could be raised by the party during the arbitral proceedings, if the matter alleged, is beyond the scope of its authority. Sub-section (4) of Section 16 gives discretionary power to arbitral tribunal to admit a later plea. It provides that the tribunal may, in either of the cases referred to in Sub-section (2) or Sub-section (3) admit a later plea if it considers the delay justified. The arbitral tribunal shall decide on a plea referred to it in Sub-section (2) or Sub-section (3) and where the tribunal takes a decision rejecting the plea, it shall continue with the arbitral proceedings and make an arbitral award. [Section 16(5)]

An application for setting aside the award may be made in the Court by a party aggrieved by such an arbitral award. The application should be made in accordance with Section 34 of the Act. If a contract is declared null or void, it does not mean that arbitration is not valid. In other words, under the Act, the clause or an arbitration agreement is to be treated as a clause or an agreement and independent from the other terms of the contract and therefore the validity of the arbitration clause or arbitration agreement is not affected by the modification or recession, invalidity or revocation of the contract.

## **Interim measures ordered by Arbitral Tribunal**

Interim measures are made in the interest of justice and the jurisdiction of the tribunal for interim measures is limited to the subject matter of dispute. Section 17 of the Act relates to interim measures ordered by the tribunal whereas Section 9 of the Act authorises a court to order interim measures. Section 17 provides that unless the parties have specifically agreed, the tribunal may order a party for taking any interim measure of protection as the tribunal may consider necessary in respect of subject matter of the dispute. For obtaining an order, an application must be made by a party. As per Sub-section (2) of Section 17 the tribunal may ask a party to provide appropriate security in connection with the protective measures ordered by it under sub-section (1) of Section 17.

Interim measures are temporary and provisional. They are operative till the dispute is resolved by an award to protect the interest of a party.

## **Arbitral award**

Section 31 of the Act lays down the requirements as to form and contents of an arbitration award. An award must be a speaking order i.e. it must state the reasons, unless the parties have specifically agreed that reasons need not be given or the award is based on agreed terms. The award should state the reasons upon which it is based. In other words, unless (a) the parties have agreed that no reasons are to be given or (b)

the award is an arbitral award on agreed terms under Section 30 of the Act, the award should state the reasons in support of determination of the liability/non-liability. The legislature has not accepted the ratio of Constitution Bench in the *Chokhamal Contractor's case* (AIR 1990 SC 1426), that the award, being in the private law field, need not be a speaking award even where the award relates to the contract of private parties or between person and the Government or public sector undertakings (*Tamil Nadu Electricity Board v. Bridge Tunnel Constructions & Others*, AIR 1997 SC 1376). Date and Place are to be mentioned in the award in accordance with Section 20 of the Act and the award should be deemed to have been made at that place.

Section 31(1) requires that the award shall be made in writing and shall be signed by the members of the arbitral tribunal. According to Sub-section (5) of Section 31 of the Act, a signed copy of the same is to be delivered to each party.

### **Interim award**

The arbitral tribunal can make an interim award on any matter with respect to which it may make a final award (See also Section 2(1)(c) of the Act).

### **Award of interest**

Section 31(7) of the Act provides as under:

- (a) Unless otherwise agreed by the parties, where and insofar as an arbitral award is for the payment of money, the arbitral tribunal may include in the sum for which the award is made, interest at such rate as it deems reasonable, on the whole or any part of the money, for the whole or any part of the period between the date on which the cause of action arose and the date on which the award is made.
- (b) A sum directed to be paid by an arbitral award shall, unless the award otherwise directs, carry interest at the rate of eighteen per cent per annum from the date of the award to the date of payment.

### **Finality of arbitral awards**

Section 35 of the Act corresponds to the Article 35(1) of UNCITRAL Model Law. The Section 35 of the Act provides that subject to the provisions of Part-I of the Act the award shall be final and binding on the parties and persons claiming under it. In other words an arbitral award is final and binding on the parties and the persons claiming under the same, subject to time limit prescribed under Sections 33 and 34 of the Act.

### **Test your knowledge**

#### **Choose the correct answer**

Which Section of the Act authorises a court to order interim measures?

- (a) Section 5
- (b) Section 9
- (c) Section 11
- (d) Section 12

**Correct answer: (b)**

### Correction and interpretation of an award

Section 33 of the Act deals with correction and interpretation of an award, or additional award.

The award may be corrected by the arbitral tribunal within 30 days of the receipt of the award. For that purpose, a party, with notice to the other party, may request the tribunal to correct any computation errors, any clerical or typographical errors or any other errors of a similar nature occurring in the award. If so agreed by the parties, a party, with notice to the other party, may request the arbitral tribunal to give an interpretation of a specific point or part of the award. Sub-section (1) of Section 33 also provides that the parties may agree upon a period of time other than 30 days for the request.

If the tribunal finds that the request is reasonable, it shall make a correction or give an interpretation, within 30 days of the receipt of the request. However, the tribunal may extend if necessary, the period of time within which it shall make a correction, give an interpretation of arbitral award under the provisions of Sub-section (6) of Section 33 of the Act. The interpretation shall be treated as part of the award. Likewise, the arbitral tribunal may also correct any errors, on its own within 30 days from the date of the award. That time cannot be extended by the tribunal.

### Additional award

Sub-section (4) of Section 33 contains provisions for making additional award. It provides that unless otherwise agreed by the parties, a party with notice to the other party, may request the tribunal to make an additional award as to claims presented in the arbitral proceedings but omitted from the arbitral award. Such request may be made within 30 days from the receipt of the arbitral award. If the arbitral tribunal considers the above request reasonable, the tribunal shall make the additional arbitral award within 60 days of the request. The time period of 60 days may be extended by the tribunal if necessary.

The provisions of Section 31 of the Act shall be applicable to a correction or an interpretation of the award or to an additional award.

### Enforcement of award

Section 36 of the Act provides that if the time for making an application to set aside the award has expired or the application has been refused, the award shall be enforced under the Code of Civil Procedure, 1908 in the same manner as it were a decree of the Court.

## PROVISIONS REGARDING SETTING ASIDE AN AWARD

The parties can approach the Court for setting aside the Award. Section 2(e) specifically provides that "Court" means the principal Civil Court of original jurisdiction in a district, including High Court and excludes any Civil Court of grade inferior to such principal Civil Court or any Court of small causes.

An application may be made in accordance with Sub-section (2) and Sub-section (3) of Section 34 of the Act for setting aside an arbitral award.

Sub-section (2) of Section 34, stipulates the following grounds on which the award may be challenged before the Court:

- (i) incapacity of a party;
- (ii) invalidity of the arbitration agreement;
- (iii) party applying was not given proper notice of the appointment of the arbitrator or of the arbitral proceedings or was otherwise unable to present his case;

- (iv) award not in accordance with the terms of submission to arbitration in regard to the dispute;
- (v) arbitral tribunal not properly constituted or the arbitral procedure was not in accordance with the agreement of the parties;
- (vi) subject matter of the dispute not capable of settlement by arbitration under the law for the time being in force;
- (vii) award being in conflict with 'the public policy of India'.

Explanation to Sub-section (2)(b) provides that an award would be in conflict with public policy if it is induced or affected by fraud or corruption or violates Section 75 or Section 81 of the Act relating to confidentiality and admissibility of evidence in other proceedings.

Section 34(3) of the Act prescribes the time limit for making an application for setting aside an arbitral award. The application cannot be made after three months have elapsed from the date on which the party making that application had received the arbitral award or if a request had been made under Section 33 from the date on which that request had been disposed of by the arbitral tribunal. It is further provided that the period of three months could be extended to a maximum of 30 days by the Court but not thereafter if the Court is satisfied that the applicant was prevented by sufficient cause from making the application within the said period.

### Interim measures by the Court

Section 9 of the Act relates to interim measures by the Court. These measures can be ordered by the Court, on an application by a party before or during the arbitral proceedings or at any time before the enforcement of an award. It is based on Section 9 of the UNICITRAL Model Law on International Commercial arbitration. The intention of the legislators in incorporating Section 9 is quite explicit that the party before arbitral proceedings or at any time after making of the award but before its enforcement can apply to the Court for interim relief. **In *Ashok Chawla v. Rakesh Gupta*, (1996) 2 Arb. L-J. 255, it has been held that in the absence of any prayer for substantive relief, the prayer for issuing any directions by way of interim measures cannot be entertained.** Section 9 contains various interim measures such as appointment of a guardian for a minor or a person of unsound mind for the purpose of arbitral proceedings or taking measures for protection of assets, issue of interim injunctions or appointment of a receiver etc. In a case, petitioner contractor entered into an agreement to execute work of building construction. The work could not be completed within time as stipulated in the agreement. Therefore, the petitioner sought injunction restraining respondents from getting construction work executed by other agency or contractors. Delhi High Court held that such building contract can not be specifically enforced by in favour of petitioner granting interim relief under Section 9 of the Act (See *BSM Contractors Pvt. Ltd. v. Rajasthan State Bridge and Construction Corporation Ltd. and another*, AIR 1999 Delhi 117).

The order of the Court is appealable under Section 37 of the Act of 1996.

### Appeals

Section 37 of the Act provides that an appeal shall lie from the following orders (and from no others) to the court authorised by law to hear appeals from original decrees of the court passing the order, namely;

- (a) granting or refusing to grant any measures under Section 9;
- (b) setting aside or refusing to set aside an arbitral award under Section 34.

An appeal may also lie against the decision of the arbitral tribunal (a) accepting the plea referred in Sub-section (2) or Sub-section (3) of Section 16 or (b) under Section 17 of the Act relating to granting or refusing to grant any interim measures. [Section 37(2)]

Section 37(3) prohibits making of second appeal from an order passed in appeal under Section 37(1) and (2) of the Act but the right to appeal to the Supreme Court is always open to a party aggrieved. The Supreme Court may in its discretion grant special leave to appeal where the needs of justice demand an interference by the highest court of the land. The power conferred upon the Supreme Court is a residuary and extraordinary. However, it shall be exercised by the Court in accordance with the well-established judicial principles or the well established norms of procedure which have been recognised for long as precedents.

### ENFORCEMENT OF FOREIGN ARBITRAL AWARDS

Chapters I and II of Part II of the Arbitration and Conciliation Act, 1996 deal with the enforcement of certain foreign awards made under the New York Convention and the Geneva Convention, respectively. Sections 44 and 53 of the Act define the foreign awards as to mean an arbitral award on differences between persons arising out of legal relationship, whether contractual or not, considered commercial under the law in force in India made on or after the 11<sup>th</sup> day of October 1960 in the case of New York Convention awards and after the 28<sup>th</sup> day of July 1924 in the case of Geneva Convention awards.

### AWARDS MADE UNDER NEW YORK CONVENTION OR GENEVA CONVENTION

Any foreign award whether made under New York Convention or Geneva Convention, which would be enforceable under the Act have been treated as binding for all purposes on the persons as between whom it was made, and may accordingly be relied on by any of those persons by way of defence, set off or otherwise in any legal proceedings in India.

In the case of **Bharat Aluminium Co. VS. Kaiser Aluminium Technical Service, Inc** on 7<sup>th</sup> September, 2012 the Supreme Court held that the Arbitration Act, 1996 has accepted the territoriality principle which has been adopted in the UNCITRAL Model Law. Section 2(2) makes a declaration that Part I of the Arbitration Act, 1996 shall apply to all arbitrations which take place within India. We are of the considered opinion that Part I of the Arbitration Act, 1996 would have no application to International Commercial Arbitration held outside India. Therefore, such awards would only be subject to the jurisdiction of the Indian courts when the same are sought to be enforced in India in accordance with the provisions contained in Part II of the Arbitration Act, 1996. In the opinion of Supreme Court, the provisions contained in Arbitration Act, 1996 make it crystal clear that there can be no overlapping or intermingling of the provisions contained in Part I with the provisions contained in Part II of the Arbitration Act, 1996 and opinion, the provision contained in Section 2(2) of the Arbitration Act, 1996 is not in conflict with any of the provisions either in Part I or in Part II of the Arbitration Act, 1996. In a foreign seated international commercial arbitration, no application for interim relief would be maintainable under Section 9 or any other provision, as applicability of Part I of the Arbitration Act, 1996 is limited to all arbitrations which take place in India. Similarly, no suit for interim injunction simplicitor would be maintainable in India, on the basis of an international commercial arbitration with a seat outside India.

In this case hon'ble Supreme Court concluded that Part I of the Arbitration Act, 1996 is applicable only to all the arbitrations which take place within the territory of India.

### Conditions for Enforcement of Foreign Awards

Section 57 of the Act enumerates the conditions for enforcement of foreign awards and provides that the party, against whom the award is invoked, may use any of the following grounds as defence before the Court for the purpose of refusal of enforcement of the foreign awards, namely:

- (i) the parties were under some incapacity under the law applicable to them or the arbitration agreement is not valid under that law; or

- (ii) the party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or
- (iii) the award deals with a difference not falling within the terms of submission to arbitration. However, if the award can be separated, the decision on the matters beyond the scope of the arbitration agreement shall not be enforced; or
- (iv) the composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties or in the law of the country where the arbitration took place; or
- (v) the award has not yet become binding, or has been set aside or suspended by a competent authority of the country in which or under the law of which, the award was made; or
- (vi) the subject-matter of the difference is not capable of settlement by arbitration under the law of India; or
- (vii) the enforcement of award would be contrary to the public policy of India. In this context, it has been clarified that an award is in conflict with the public policy of India if the making of the award is induced or effected by fraud or corruption.

The provisions regarding conditions for enforcement of foreign awards made under the New York Convention or the Geneva Convention are almost the same. It is obligatory on the party applying for the enforcement of a foreign award to produce before the Court:

- (a) the original award or a duly authenticated copy thereof;
- (b) the original agreement for arbitration or a duly-certified copy thereof; and
- (c) such evidence as may be necessary to prove that the award is a foreign award.

Where the award or agreement is in a foreign language, the party seeking to enforce the award is required to produce a certified translated copy in English. Where the Court is satisfied that the foreign award is enforceable, the award shall be deemed to be a decree of that Court.

### **Appealable Orders**

An appeal to the Court authorized by law to hear appeals from such order, may lie on the following two counts:

- (i) Where the judicial authority in India has ordered refusing to refer the parties to arbitration under Section 45 in case the New York Convention is applicable to them under Section 54 in case the Geneva Convention is applicable to them.

The aforesaid sections i.e. Section 45 and Section 54 provide that a judicial authority, when seized of an action in a matter in respect of which the parties have made an agreement referred in Section 44 or Section 53, shall, at the request of one of the parties or any person claiming through or under him, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed.

- (ii) Where the Court has refused to enforce a foreign award either under Section 48 or Section 57 of the Act.

Section 50(2) prohibits a second appeal from an order passed in appeal. However, any right of the parties to appeal to the Supreme Court shall not be affected or taken away by virtue of these provisions.

Both the Chapters of Part II dealing with New York Convention awards and Geneva Convention awards contain a similar saving provision which provides that nothing in this chapter shall prejudice

any rights which any person would have had of enforcing in India of any award or of availing himself in India of any award if this chapter had not been enacted.

## CONCILIATION

 Conciliation is an informal process in which the conciliator (the third party) tries to bring the disputants to agreement. He does this by lowering tensions, improving communications, interpreting issues, providing technical assistance, exploring potential solutions and bringing about a negotiated settlement. Mediation is a structured process in which the mediator assists the disputants to reach a negotiated settlement of their differences. Mediation is usually a voluntary process that results in a signed agreement which defines the future behaviour of the parties. The mediator uses a variety of skills and techniques to help the parties reach the settlement, but is not empowered to render a decision.

Basically, these processes can be successful only if the personality of the conciliator or the mediator is such that he is able to induce the parties to come to a settlement. The Act gives a formal recognition to conciliation in India. Conciliation forces earlier and greater hold of the case. It can succeed only if the parties are willing to re-adjust. According to current thinking conciliation is not an alternative to arbitration or litigation, but rather complements arbitration or litigation.

### ***Differences between Arbitration and Conciliation***

Arbitration and conciliation differ in some major ways:

- In arbitration, the decision is known as arbitral award and is signed by the arbitral tribunal members; while under conciliation, it is known as settlement and is signed by the parties concerned.
- In arbitration, parties cannot appoint even number of arbitrators; while in conciliation, the number of conciliators can be even.

Arbitrators can be appointed even before the dispute arises; while a conciliator is appointed only after the dispute has arisen.

### **Application and scope of conciliation**

(1) Save as otherwise provided by any law for the time being in force and unless the parties have otherwise agreed, this Part shall apply to conciliation of disputes arising out of legal relationship, whether contractual or not and to all proceedings relating thereto.

(2) This Part shall not apply where by virtue of any law for the time being in force certain disputes may not be submitted to conciliation. (Section 61)

### **Commencement of conciliation proceedings**

(1) The party initiating conciliation shall send to the other party a written invitation to conciliate under this Part, briefly identifying the subject of the dispute.

(2) Conciliation proceedings shall commence when the other party accepts in writing the invitation to conciliate.

(3) If the other party rejects the invitation there will be no conciliation proceedings.

(4) If the party initiating conciliation does not receive a reply within thirty days from the date on which he sends the invitation, or within such other period of time as specified in the invitation he may elect to treat this

as a rejection of the invitation to conciliate and if he so elects, he shall inform in writing the other party accordingly. (Section 62)

### **Number of conciliators**

- (1) There shall be one conciliator unless the parties agree that there shall be two or three conciliators.
- (2) Where there is more than one conciliator, they ought, as a general rule, to act jointly. (Section 63)

### **Appointment of Conciliators**

- (1) Subject to Sub-section (2) of Section 64:
  - (a) in conciliation proceedings with one conciliator, the parties may agree on the name of a sole conciliator;
  - (b) in conciliation proceedings with two conciliators, each party may appoint one conciliator;
  - (c) in conciliation proceedings with three conciliators, each party may appoint one conciliator and the parties may agree on the name of the third conciliator who shall act as the presiding conciliator.
- (2) Parties may enlist the assistance of a suitable institution, or person in connection with the appointment of conciliators, and in particular:
  - (a) a party may request such an institution or person to recommend the names of suitable individuals to act as conciliator; or
  - (b) the parties may agree that the appointment of one or more conciliators be made directly by such an institution or person:

Provided that in recommending or appointing individuals to act as conciliator, the institution or person shall have regard to such considerations as are likely to secure the appointment of an independent and impartial conciliator and, with respect to a sole or third conciliator, shall take into account the advisability of appointing a conciliator of a nationality other than the nationalities of the parties. (Section 64)

### **Submission of statements to conciliator**

- (1) The conciliator, upon his appointment, may request each party to submit to him a brief written statement describing the general nature of the dispute and the points at issue. Each party shall send a copy of such statement to the other party.
- (2) The conciliator may request each party to submit to him a further written statement of his position and the facts and grounds in support thereof, supplemented by any documents and other evidence that such party deems appropriate. The party shall send a copy of such statement, documents and other evidence to the other party.
- (3) At any stage of the conciliation proceedings, the conciliator may request a party to submit such additional information as he deems appropriate. (Section 65)

*Explanation:* In this Section and all the following Sections of this part, the term "conciliator" applies to a sole conciliator, two or three conciliators as the case may be.

### **Conciliator not bound by certain enactments**

The conciliator is not bound by the Code of Civil Procedure, 1908 or the Indian Evidence Act, 1872. (Section 66)

Conciliator is vested with wide powers to decide the procedure to be followed by him untrammelled by the procedural laws like the Code of Civil Procedure or the Indian Evidence Act 1872 (See *Haresh Dayaram v. State of Maharashtra*, AIR 2000 SC 2285).

### **Role of conciliator**

- (1) The conciliator shall assist the parties in an independent and impartial manner in their attempt to reach an amicable settlement of their dispute.
- (2) The conciliator shall be guided by principles of objectivity, fairness and justice, giving consideration to, among other things, the rights and obligations of the parties, the usages of the trade concerned and the circumstances surrounding the dispute, including any previous business practices between the parties.
- (3) The conciliator may conduct the conciliation proceedings in such a manner as he considers appropriate, taking into account the circumstances of the case, the wishes the parties may express, including any request by a party that the conciliator hear oral statements, and the need for a speedy settlement of the dispute.
- (4) The conciliator may, at any stage of the conciliation proceedings, make proposals for a settlement of the dispute. Such proposals need not be in writing and need not be accompanied by a statement of the reasons therefor. (Section 67)

### **Administrative assistance**

In order to facilitate the conduct of the conciliation proceedings, the parties, or the conciliator with the consent of the parties, may arrange for administrative assistance by a suitable institution or person. (Section 68)

### **Communication between conciliator and parties**

- (1) The conciliator may invite the parties to meet him or may communicate with them orally or in writing. He may meet or communicate with the parties together or with each of them separately.
- (2) Unless the parties have agreed upon the place where meetings with the conciliator are to be held, such place shall be determined by the conciliator, after consultation with the parties, having regard to the circumstances of the conciliation proceedings. (Section 69)

### **Disclosure of Information**

When the conciliator receives factual information concerning the dispute from a party, he shall disclose the substance of that information to the other party in order that the other party may have the opportunity to present any explanation which he considers appropriate:

Provided that when a party gives any information to the conciliator subject to a specific condition that it be kept confidential, the conciliator shall not disclose that information to the other party. (Section 70)

### **Co-operation of parties with Conciliator**

The parties shall in good faith co-operate with the conciliator and, in particular, shall endeavour to comply with requests by the conciliator to submit written materials, provide evidence and attend meetings. (Section 71)

### **Suggestions by parties for settlement of dispute**

Each party may, on his own initiative or at the invitation of the conciliator, submit to the conciliator suggestions for the settlement of the dispute. (Section 72)

### **Settlement agreement**

- (1) When it appears to the conciliator that there exists elements of a settlement which may be acceptable to

the parties, he shall formulate the terms of a possible settlement and submit them to the parties for their observations. After receiving the observations of the parties, the conciliator may reformulate the terms of a possible settlement in the light of such observations.

(2) If the parties reach agreement on a settlement of the dispute, they may draw up and sign a written settlement agreement. If requested by the parties, the conciliator may draw up, and assist in drawing up, the settlement agreement.

(3) When the parties sign the settlement agreement, it shall be final and binding on the parties and persons claiming under them respectively.

(4) The conciliator shall authenticate the settlement agreement and furnish a copy thereof to each of the parties. (Section 73)

### **Status and effect of settlement agreement**

The settlement agreement shall have the same status and effect as if it is an arbitral award on agreed terms on the substance of the dispute rendered by an arbitral tribunal under Section 30. (Section 74)

Under Sub-section (3) of Section 73, a successful conciliation proceedings comes to an end only when the settlement agreement signed by the parties comes into existence. It is such an agreement which has the status and effect of legal sanctity of an arbitral award under Section 74 of the Act (*Haresh Dayaram Thakur v. State of Maharashtra*, AIR 2000 SC 2281).

### **Confidentiality**

Notwithstanding anything contained in any other law for the time being in force, the conciliator and the parties shall keep confidential all matters relating to the conciliation proceedings. Confidentiality shall extend also to the settlement agreement, except where its disclosure is necessary for purposes of implementation and enforcement. (Section 75)

### **Termination of conciliation proceedings**

The conciliation proceedings shall be terminated:

- (a) by the signing of the settlement agreement by the parties on the date of the agreement; or
- (b) by a written declaration of the conciliator, after consultation with the parties, to the effect that further efforts at conciliation are no longer justified, on the date of the declaration; or
- (c) by a written declaration of the parties addressed to the conciliator to the effect that the conciliation proceedings are terminated, on the date of the declaration; or
- (d) by a written declaration of a party to the other party and the conciliator, if appointed, to the effect that the conciliation proceedings are terminated, on the date of the declaration. (Section 76)

### **Resort to arbitral or judicial proceedings**

The parties shall not initiate, during the conciliation proceedings, any arbitral or judicial proceedings in respect of a dispute that is the subject matter of the conciliation proceedings except that a party may initiate arbitral or judicial proceedings where, in his opinion, such proceedings are necessary for preserving his rights. (Section 77)

### **Costs**

(1) Upon termination of the conciliation proceedings, the conciliator shall fix the costs of the conciliation and give written notice thereof to the parties.

(2) For the purpose of Sub-section (1), "costs" means reasonable costs relating to:

- (a) the fee and expenses of the conciliator and witnesses requested by the conciliator with the consent of the parties;
- (b) any expert advice requested by the conciliator with the consent of the parties;
- (c) any assistance provided pursuant to clause (b) of Sub-section (2) of Section 64 and Section 68;
- (d) any other expenses incurred in connection with the conciliation proceedings and the settlement agreement.

(3) The costs shall be borne equally by the parties unless the settlement agreement provides for a different apportionment. All other expenses incurred by a party shall be borne by that party. (Section 78)

### **Deposits**

(1) The conciliator may direct each party to deposit an equal amount as an advance for the costs referred to in Sub-section (2) of Section 78 which he expects will be incurred.

(2) During the course of the conciliation proceedings, the conciliator may direct supplementary deposits in an equal amount from each party.

(3) If the required deposits under Sub-sections (1) and (2) are not paid in full by both the parties within thirty days, the conciliator may suspend the proceedings or may make a written declaration of termination of the proceedings to the parties, effective on the date of that declaration.

(4) Upon termination of the conciliation proceedings, that conciliator shall render an accounting to the parties of the deposits received and shall return any unexpected balance to the parties. (Section 79)

### **Role of Conciliator in other proceedings**

Unless otherwise agreed by the parties:

- (a) the conciliator shall not act as an arbitrator or as a representative or counsel of a party in any arbitral or judicial proceedings in respect of a dispute that is the subject of the conciliation proceedings.
- (b) the conciliator shall not be presented by the parties as a witness in any arbitral or judicial proceedings. (Section 80)

### **Admissibility of evidence in other proceedings**

The parties shall not rely on or introduce as evidence in arbitral or judicial proceedings, whether or not such proceedings relate to the dispute that is the subject of the conciliation proceedings:

- (a) views expressed or suggestions made by the other party in respect of a possible settlement of the dispute;
- (b) admissions made by the other party in the course of the conciliation proceedings;
- (c) proposals made by the conciliator;
- (d) the fact that the other party had indicated his willingness to accept a proposal for settlement made by the conciliator. (Section 81)

**Test your knowledge**

How can the conciliation proceedings be terminated?

- By the signing of the settlement agreement by the parties on the date of the agreement
- By a written declaration of the conciliator, after consultation with the parties, to the effect that further efforts at conciliation are no longer justified, on the date of the declaration
- By a written declaration of the parties addressed to the conciliator to the effect that the conciliation proceedings are terminated, on the date of the declaration
- By oral agreement

**Correct answer: (a), (b) and (c)**

**ALTERNATIVE DISPUTE RESOLUTION (ADR)**

There is a growing awareness that courts will not be in a position to bear the entire burden of justice system. A very large number of disputes lend themselves to resolution by alternative modes such as arbitration, mediation, conciliation, negotiation, etc. The ADR processes provide procedural flexibility save valuable time and money and avoid the stress of a conventional trial.

At present, ADR services are offered in India in very rudimentary form. There is, therefore, an urgent need to establish and promote ADR services for resolution of both domestic and international disputes in India. These services need to be nourished on sound conceptions, expertise in their implementation and comprehensive and modern facilities.

The International Centre for Alternative Dispute Resolution (ICADR) is a unique centre in this part of the world that makes provision for promoting teaching and research in the field of ADR as also for offering ADR services to parties not only in India but also to parties all over the world. The ICADR is a Society registered under Societies Registration Act, 1860, it is an independent non-profit making organisation. It maintains panels of independent experts in the implementation of ADR processes.

**Areas in which ADR works**

Almost all disputes including commercial, civil, labour and family disputes, in respect of which the parties are entitled to conclude a settlement, can be settled by an ADR procedure. ADR techniques have been proven to work in the business environment, especially in respect of disputes involving joint ventures, construction projects, partnership differences, intellectual property, personal injury, product liability, professional liability, real estate, securities, contract interpretation and performance and insurance coverage.

**LESSON ROUND UP**

- The purpose of Arbitration Act is to provide quick redressal to commercial disputes by private arbitration. The Arbitration and Conciliation Act, 1996 aims at streamlining the process of arbitration and facilitating conciliation in business matters.
- The Act has been divided into four parts. Part one deals with Arbitration; Part two deals with enforcement of certain Foreign Awards; Part three deals with conciliation; and Part four contains supplementary provisions.
- The Act contains three Schedules. Schedule one contains provisions relating to convention on the Recognition and Enforcement of Foreign Arbitral Awards; Schedule two deals with Protocol on Arbitration Clauses and Schedule three contains provisions relating to Execution of Foreign Arbitral Awards.

- The Act is based on model law drafted by United Nations Commission on International Trade Laws (UNCITRAL), both on domestic arbitration as well as international commercial arbitration, to provide uniformity and certainty to both categories of cases.
  - Conciliation is an informal process in which the conciliator (the third party) tries to bring the disputants to agreement. He does this by lowering tensions, improving communications, interpreting issues, providing technical assistance, exploring potential solutions and bringing about a negotiated settlement. Mediation is a structured process in which the mediator assists the disputants to reach a negotiated settlement of their differences.
  - Mediation is usually a voluntary process that results in a signed agreement which defines the future behaviour of the parties. The mediator uses a variety of skills and techniques to help the parties reach the settlement, but is not empowered to render a decision.
  - The Alternative Dispute Resolution (ADR) processes provide procedural flexibility save valuable time and money and avoid the stress of a conventional trial. The International Centre for Alternative Dispute Resolution (ICADR) is a unique centre in this part of the world that makes provision for promoting teaching and research in the field of ADR as also for offering ADR services to parties not only in India but also to parties all over the world.

## **SELF TEST QUESTION**

1. What are the grounds to challenge the appointment of an Arbitrator under the Arbitration and Conciliation Act, 1996? Discuss.
  2. What do you understand by an arbitration agreement? What are its essentials?
  3. What are the grounds for setting aside of an arbitral award under the Arbitration and Conciliation Act, 1996?
  4. What are the provisions relating to settlement of the dispute under the Arbitration and Conciliation Act, 1996?
  5. Part I of the Arbitration and Conciliation Act, 1996 applicable only to all the arbitrations which take place within the territory of India. Give your answer with decided case study.

# Lesson 6

## LAW RELATING TO TRANSFER OF PROPERTY

### LESSON OUTLINE

- Important Definitions
- Distinction between Moveable and Immoveable Property
- Rules relating to Transfer of Property
- Who can transfer the Property
- Subject matter of Transfer
- Rules against Inalienability
- Transfer for benefit of Unborn Person
- Conditional Transfer
- Doctrine of Election
- Doctrine of Holding Out
- Doctrine of Feeding the Grant by Estoppel
- Doctrine of Fraudulent Transfer
- Doctrine of Part-Performance
- Properties which cannot be Transferred
- Rule against Perpetuity
- Accumulation of Income
- Doctrine of Lis Pendens
- Provisions relating to Specific Transfers
- Actionable Claims
- Charges

### LEARNING OBJECTIVES

Article 17 of Universal Declaration on Human Rights provides that everyone has the right to own property alone as well as in association with others and no one shall be arbitrarily deprived of his property. As per Article 300A of Constitution of India, persons not to be deprived of property save by authority of law.

Property has, always, been on the fundamental elements of socio economic life of an individual. Transfer of Property means an act by which a living person conveys property in present, or in future, to one or more other living persons, or to himself and one or more other living persons and "to transfer property" is to perform such an act. Consequently, the law relating to transfer of property is not only an important branch of civil law but also one that demands proper elucidation due to its complexity.

Therefore, students should be well versed in this subject so as to understand the intricacies involved in the transfer of property.

The law relating to transfer of property is governed by the Transfer of Property Act, 1882. The very preamble to the Act suggests that it simply defines and amends certain parts of the law relating to transfer of property by act of parties.

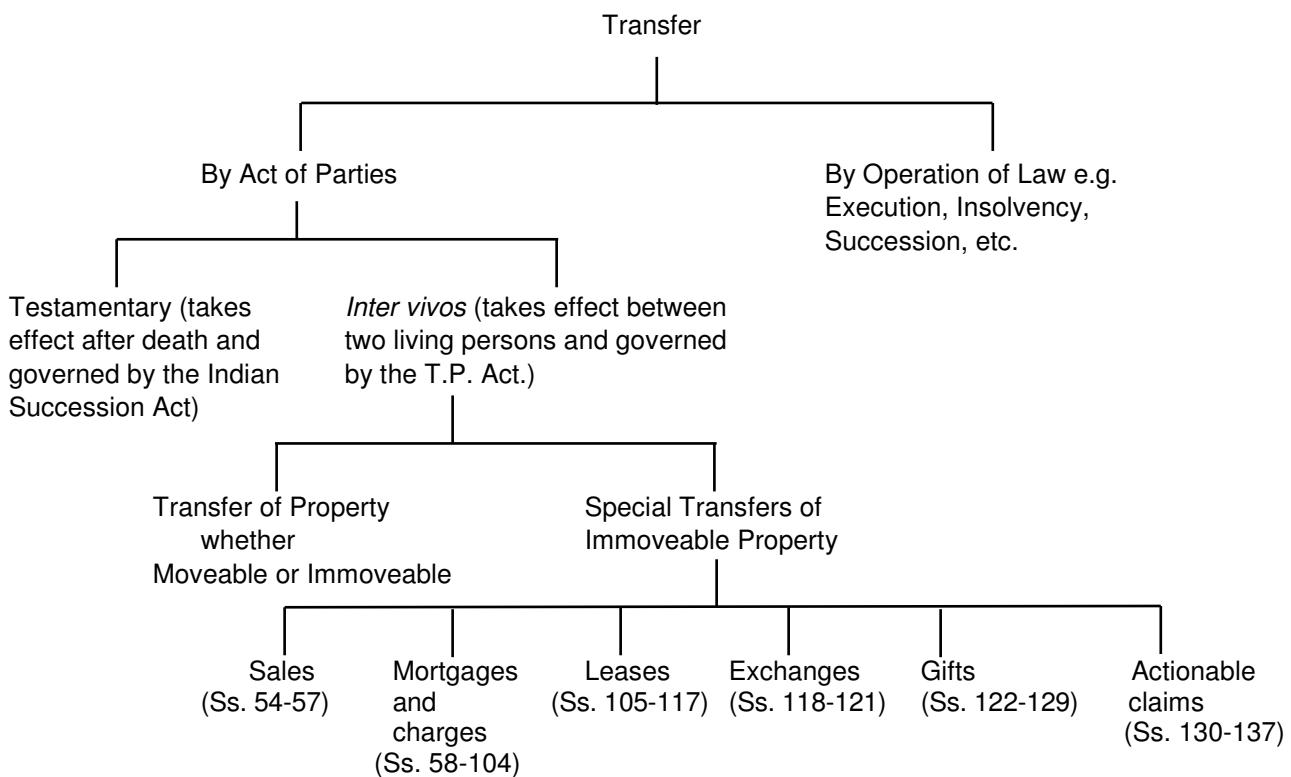
## INTRODUCTION

The law relating to transfer of property is governed by the Transfer of Property Act, 1882. Before this Act came into force there was practically no law as to real property in India. Barring few points which were covered by certain Regulations and Acts, the Courts in India in the absence of any statutory provisions, applied rules of English law as the rule of *justice, equity and good conscience*.

The Act was enacted with the object to *amend the law relating to the transfer of property by act of parties*. The Act excludes from its purview the transfers by operation of law, i.e. by sale in execution, forfeiture, insolvency or intestate succession. The scope of the Act is limited, as it is confined to transfers *inter vivos* and excludes testamentary succession, i.e. transfers *by will*.

The very preamble to the Act suggests that it simply defines and amends certain parts of the law relating to transfer of property by act of parties, and it does not at all profess to be an exhaustive enactment as is revealed by the omission of the word "*consolidate*". Therefore, the Act leaves the scope for applying rules of *justice, equity and good conscience* if a particular case is not covered by any of the provisions of the Act. But if it is covered, the Act must be applied.

## SCHEME OF THE ACT



## IMPORTANT DEFINITIONS

However, while explaining the provisions of the Act, the terms used are defined there itself, yet some of the important terms used under the Act are as follows:

### **Instrument**

"Instrument" means a non-testamentary instrument.

**Attached to the earth**

Attach to the earth means:

- (a) rooted in the earth, as in the case of trees and shrubs;
- (b) imbedded in the earth, as in the case of walls or buildings; or
- (c) attached to what is so embedded for the permanent beneficial enjoyment of that to which it is attached.

**Absolute Interest**

When a person owns property, he has an "absolute interest" in the property. Ownership consists of a bundle of rights, the right to possession, right to enjoyment and right to do anything such as selling, mortgaging or making gift of the property. If A is the owner of a land, he has an absolute interest in the land. If A sells his land to B, then B becomes the owner and he acquires an absolute interest in the land he has purchased from A. Likewise if A makes a gift of his property to B, there again B gets an absolute interest in the property which is gifted to him. These are instances where persons may have an absolute interest.

**Reversion and Remainder**

Some interests in the property are called in English Law, reversion and remainders. A "reversion" is the residue of an original interest which is left after the grantor has granted the lessee a small estate. For example, A, the owner of a land may lease it to B for a period of five years. The person who grants the lease is the lessor and the person who takes the lease is called the lessee. Here, after the period of 5 years the lease will come to an end and the property reverts back to the lessor. The property which reverts back to him is called the reversion or the reversionary interest. The grantor has a larger and an absolute interest out of which he carves out a smaller estate and gives to the grantees, i.e. the lessee.

When the owner of the property grants a limited interest in favour of a person or persons and gives the remaining to others, it is called a "remainder". For instance, A the owner of a land transfers property to B for life and then to C absolutely. Here the interest in favour of B is a limited interest, i.e., it is only for life. So long as A is alive he enjoys the property. He has a limited right since he cannot sell away the property. His right is only to enjoy the property. If he sells this interest it will be valid so long as he is alive. So after B's death the property will go to C, interest is called a remainder. In the case of a "remainder", the property will not come back to the owner, but it goes over to the other person.

**Vested and Contingent Interests**

The word "vested" is used in two different senses. It may mean "vested in possession" or "vested in interest". A right is said to be "vested in possession" when it is a right to present possession of property and it is said to be "vested in interest" when it is not a right to present possession but a present right to future possession. For instance, if a land is given to A for life with a remainder to B, A's right is vested in possession, B's right is vested in interest. In the above example, the interest of B is not subject to any uncertain condition. It will come into his possession after A's life comes to an end. Therefore, an interest is said to be vested when it is not subject to any condition, precedent, i.e., when it is to take effect on the happening of an event which is certain, whereas an estate is contingent when the right to enjoyment depends upon the happening of an event which may or may not happen. Thus, a gift to A on the death of B creates a vested interest in A even during the life time of B for there is nothing more certain than death. But a gift to A on the marriage of B creates a contingent interest, for B may never marry at all but that contingent interest becomes vested if and when B marries.

A vested interest is transferable and heritable. If property is given to A for life and afterwards to B, B gets a vested interest and if B transfers this interest to C, C will take when the life estate of A comes to an end. B's interest, since it is vested, is also heritable. Therefore, if B dies during the lifetime of A, C will get the property after the death of A.

A contingent interest, as said above, is an interest which takes effect after the condition is satisfied. It is subject to a condition precedent, i.e., unless A marries B's daughter, he will not get the property. The following example will illustrate this point. Property is given to A for life and then to B if he marries C. B should marry C before A dies. If he does so, his interest is converted into vested interest. Before B marries C his interest is contingent. The contingent interest is not heritable although it is transferable. In a vested interest the transfer is complete, but when the interest is contingent the transfer depends upon a condition precedent. In a condition precedent the estate is not vested in the grantee until the condition is fulfilled.

*Distinction between a vested and a contingent interest:* The following are the principal points of distinction between a vested and a contingent interest:

1. When an interest is vested the transfer is complete. It creates an immediate proprietary interest in the property though the enjoyment may be postponed to a future date. A contingent interest on the other hand is dependant upon the fulfilment of some conditions which may or may not happen. In other words, in case of vested interest, the owner's title is already perfect; in case of a contingent interest, the title is as yet imperfect but may become perfect on the fulfilment of a stipulated condition.
2. A vested interest takes effect from the date of transfer. A contingent interest in order to become vested is conditioned by a contingency which may not occur.
3. A vested interest cannot be defeated by the death of the transferee before he obtains possession. A contingent interest may fail in case of the death of transferee before the fulfilment of condition.
4. Since vested interest is not circumscribed by any limitation which derogates from the completeness of the grant, it logically follows that a vested interest is transferable as well as heritable. If, therefore, a transferee of the vested interest dies before actual enjoyment, it will devolve on his legal heirs. A contingent interest, on the other hand, cannot be inherited though it may be transferred coupled with limitation regarding fulfilment of a condition.

### ***Test your knowledge***

***State the following as "True" or "False"***

*A right is said to be 'vested in interest' when it is a right to present possession of property*

- *True*
- *False*



***Correct Answer: False***

## **MOVEABLE AND IMMOVEABLE PROPERTY**

The term "property" signifies the subject matter over which the right of ownership or any less right carved out of ownership (e.g. mortgage right) is exercised. The Act deals with (i) various specific transfers relating to Immoveable property and (ii) lays down general principles relating to transfer of both moveable and

immoveable property. Chapter II of the Act is divided into two parts. Parts A deals with the rules pertaining to both moveable and immoveable property (Section 5 to 37), Part B embodies the rules relating to immoveable property (Section 38 to 53A). The other chapters of the Act deal with transfers such as sales, mortgages, leases, gifts, exchanges and actionable claims. The rules relating to these transactions are referred to as rules governing special transfers to immoveable property. The fundamental rule relating to all transfers is that a transfer cannot be effected in any other way except as prescribed under the Act. Furthermore, the Act states that certain kinds of property cannot be transferred at all.

The first task is to define and distinguish between moveable and immoveable property.

### ***Moveable property***

The Transfer of Property Act does not define the term "moveable property". Therefore, it is to be defined with the help of other statutes. For e.g., it has been defined in the General Clauses Act, 1897 as to mean "property of every description except immoveable property". The Registration Act defines "moveable property" to include property of every description excluding immoveable property but including standing timber, growing crops and grass.

For the purpose of law, moveable property is sometimes regarded as immoveable property. This may happen when a thing of chattel is attached or embedded in earth. For instance, if a machinery or a plant is installed on the land, the question arises whether the machinery or the plant is moveable property or immoveable property. In order to find out whether such a thing or chattel is an immoveable property or not, it is to find out the mode of annexation of the thing and the object or purpose of such annexation. If the machinery is fixed on the land permanently then it becomes immoveable property, whereas if the machinery or engine or any other thing is fixed on a temporary basis, then it will be regarded as moveable property. Thus, where the owner of a piece of land installed a bone mill along with machinery being held by iron bars which have been dug to a considerable depth then it is a permanent fixture and this will become immoveable property. Similarly, the machinery installed on a cement platform and held in position by being attached to iron pillars fixed in the ground was held to be immoveable property as the annexation was made by the person who owned the buildings as well as the machinery (*Mohamed Ibrahim v. Northern Circars Fibre Trading Company*, A.I.R. 1944 Mad. 492).

### ***Immoveable property***

The term "immoveable property" is also not defined under the Act. However, it is defined in the negative sense as "the immoveable property *does not include standing timber, growing crops, or grass*" (S. 3 Para 2). Standing timber are trees fit for use for building or repairing houses. This is an exception to the general rule that growing trees are immoveable property.

**Growing crops:** It includes all vegetable growths which have no existence apart from their produce such as pan leaves, sugar cane etc.

**Grass:** Grass is moveable property, but if it is a right to cut grass it would be an interest in land and hence forms immoveable property.

The General Clauses Act defines the term "immoveable property" but not exhaustively. It states: "immoveable property shall include land, benefits to arise out of land and things attached to the earth, or permanently fastened to any thing attached to the earth" [Section 3(25)]. The Indian Registration Act expressly includes under to immoveable property the benefits to arise out of land, hereditary allowances, rights of way, lights, ferries and fisheries.

If the definitions of "immoveable property" as given in the Transfer of Property Act, the General Clauses Act

and the Registration Act are viewed together, it is evident that they do not say what immoveable property is. They only say what is either included or excluded therein. Still, reading the definition in the Act with one in the General Clauses Act, *immoveable property will be found to include land, benefit to arise out of land such as rent, and things attached to the earth like trees and buildings but not standing timber, growing crops and grass*. The last three things are regarded as severable from the land on which they stand and, therefore, they are not included in the term "immoveable property".

**Thus, the meaning of immoveable property is as under:**



"*Immoveable property*" means land, benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth.

"*Attached to the earth*" means (a) rooted in the earth, as in the case of trees and shrubs; (b) embedded in the earth, as in the case of walls or buildings; or (c) attached to what is so embedded for the permanent beneficial enjoyment of that to which it is attached (S. 3 Para 6 of the Act).

*Things rooted in the earth:* Trees and Shrubs are immoveable property according to this definition subject to the exception as to standing timber.

*Things embedded in the earth:* A house being embedded in the earth is immoveable property and this is so even if it is sold for enjoyment as a house with an option to pull it down. The mode of annexation and object of annexation are the two tests to determine whether it is immoveable property or not.

*Attached to what is so....:* The attachment must be as the Section says for the permanent beneficial enjoyment of that to which it is attached e.g. the doors, windows of a house or moveable parts of fixed machinery. But the attachment must be intended to be permanent.

A orally grants to B for Rs. 700/- the rights to catch and carry away fish from his lake. Is the grant valid? The Supreme Court in *Ananda Behra v. State of Orissa*, (1956) SCJ p. 96, that such a right is a benefit arising out of immoveable property namely the lake. So under General Clauses Act it is immoveable property. The sale requires a registered instrument for its validity under Section 54 of the Transfer of Property Act. Therefore, the oral grant is invalid and cannot pass away any title in favour of B.

#### **Distinction between moveable and immoveable property**



*The distinction between moveable and immoveable property was explained in the case of Sukry Kurdepa v. Goondakull, (1872) 6 Mad. H.C. 71, by Holloway J. as moveability may be defined to be a capacity in a thing of suffering alteration. Immoveability for such alteration e.g., a piece of land in all circumstances is immoveable. If a thing cannot change its place without injury to the quality it is immoveable. Certain things e.g. trees attached to the ground are so long as they are so attached, immoveable when the severance has been effected they become moveable.*

**The following have been recognised as immoveable property:**

- right to collect rents of immoveable property;
- a right to way;
- a right to collect dues from fair on a piece of land;
- hereditary offices;

- (e) the equity of redemption;
- (f) the interest of mortgagee;
- (g) right to collect lac from trees;
- (h) a right of ferry;
- (i) a right of fishery;
- (j) right to receive future rents and profits of land;
- (k) reversion in property leased;
- (l) a factory.

**The following have been held not to be immoveable property:**

- (a) right of worship;
- (b) government promissory notes;
- (c) royalty;
- (d) a right to recover maintenance allowance;
- (e) copyright;
- (f) a decree for sale on a mortgage-deed;
- (g) a decree for arrears of rent;
- (h) a machinery which is not permanently attached to earth;
- (i) standing timber, growing crop and grass.

### ***Test your knowledge***

*Which of the following properties cannot be considered as immovable?*

- (a) Growing trees
- (b) Standing timber
- (c) Growing crops
- (d) Grass

***Correct Answer: (b), (c) and (d)***



### **RULES RELATING TO TRANSFER OF PROPERTY (WHETHER MOVEABLE OR IMMOVEABLE)**

According to Section 5 of the Transfer of Property Act, the term "transfer of property" means an act by which a living person conveys property in present, or in future, to one or more other living persons, or to himself, and one or more other living persons and "to transfer property" is to perform such an act. In this section, "living person" includes a company or association or body of individuals whether incorporated or not. But the general provisions of the Act as to transfer do not effect the special provisions of the Companies Act, 1956.

To effect a transfer, property must be in existence. The word "transfer" is defined with reference to the word "convey". The fundamental rule is that a transfer cannot be affected in any way not prescribed by the Act.

The first point to note is that transfer *inter vivos* (i.e., between living persons) alone is contemplated by the Act. A transfer by means of a will is not a transfer according to the Act, because it is not a transfer between two living persons. Section 5 also says that the transfer may be "in present or in future". The words in present or in future qualify the words 'conveys', and not the word 'property'. **A transfer of property not in existence operates as a contract to be performed in future which may be specially enforced as soon as the property comes into existence (*Jugalkishore v. Ram Cotton Company*, (1955) 1 SCR 1369).**

Further Section 6 (h) provides that no transfer can be made in so far as it is opposed to the nature of the interest attached thereby or for an unlawful object or consideration or to a person legally disqualified to be a transferee.

### WHO CAN TRANSFER THE PROPERTY?

According to Section 7 of the Transfer of Property Act, every person who is competent to contract and entitled to transferable property, or authorised to dispose of property is competent to transfer such property. Hence, every person competent to contract and having ownership can transfer property. According to Indian Contract Act, a person is competent to contract when he is a major and of sound mind and is not disqualified from contracting by any law to which he is subject. But a minor can be a transferee as there is nothing in the Transfer of Property Act to disqualify a person, who is a minor to be a transferee. Thus, a mortgage can be validly executed in favour of a minor who has paid the consideration (*Hari Mohan v. Mohini*, 22 C.W.C. 130, *Raghava v. Srinivasa*, (1917) 60 Mad. 308). Persons who are authorised to transfer property can also transfer property validly. Although a minor is not competent to be a transferor yet a transfer to a minor is valid. However, there are exceptions to this:

If a person holds himself out as the owner with the consent of the owner i.e. doctrine of holding out or if a person represents to be the owner i.e. doctrine of feeding the grant by estoppel.

### SUBJECT MATTER OF TRANSFER

Section 6 of the Transfer of Property Act says that property of any kind may be transferred except as provided by this Act or any other law for the time being in force. The words "property of any kind" indicate that transferability is the general rule and the right to property includes the right to transfer the property to another person. Property of any kind excludes from its purview the future property. A transfer of future property can only operate as a contract which may be specifically performed when the property comes into existence.

#### ***Exceptions to the general rule of transferability made by other laws***

Certain restrictions are placed by Hindu law and Mohammedan law on the transfer of property.

### FORMALITIES OF TRANSFER

Property can be transferred either orally or by writing. Moveable property can be transferred by delivery of possession or by registration. Section 54 lays down the mode of transfer of immoveable property. Such transfer, in the case of *tangible* immoveable property of the value of one hundred rupees and upwards, or in the case of a *reversion* or other *intangible* thing, can be made only by a registered instrument.

In the case of *tangible* immoveable property of a value less than one hundred rupees, such transfer may be made either by a registered instrument or by delivery of the property.

The *tangible* property means a property which can be touched physically and hence, capable of physical dealing.

The *intangible* property means something in abstract, either capable of being touched or perceived and yet standing in relation to a certain thing.

'*Reversion*' means the bundle of rights remaining with the lessor after the execution of a lease of a certain immoveable property.

When a transfer is effected in writing, the person who signs the document professing to transfer the property is called the executant. Execution consists in affixing his signature to the document to the effect that he is transferring the property. An illiterate person who cannot write may direct some literate person to sign it on his behalf and in his presence and the illiterate person may put his thumb impression.

### **(i) Attestation**

Attestation is an important formality in connection with the execution of transfer. "Attest" means to testify a factor, to bear witness to a fact. Attestation, in relation to a document, signifies the fact of authentication of the signature of the executant of that document by the attestator by putting down his own signature on the document in testimony of the fact of its execution. All transfers do not require attestation. For example, a sale or a lease does not require attestation. But a mortgage or a gift requires that a mortgage deed or a gift deed must be attested by two or more witnesses.

Attestation is valid and complete when two witnesses sign the instrument. According to the definition given in the Transfer of Property Act (Section 3), the following essentials are required for a valid attestation:

- (a) There must be at least two or more witnesses;
- (b) Each witness must see (a) the executant's sign or affix his mark to the instrument, or (b) some other person sign the instrument in the presence and by the direction of the executant, or (c) receive from the executant a personal acknowledgement of his signature or mark or of the signature of such other person; and
- (c) Each witness must sign the instrument, (i.e. document), in the presence of the executant.

It is not necessary that both attesting witnesses should be present at the same time. The instrument may be attested after its execution by each of the attestors at different times. Attestation cannot take place before the execution of the deed. The Act does not insist on any particular form of attestation. The attesting witness may not be described as such on the face of the document (*Yakub v. Kalzurkan*, 52 Bombay 203). However, the attesting witness must have put his signature *antmus attestandi*, i.e., with intention to attest. Thus, where a Register or an identifying witness puts his signature on the document he cannot be regarded as an attesting witness unless it is duly proved that he signed with the necessary intention to attest.

### **(ii) Registration**

Registration is an essential legal formality to effect a valid transfer in certain cases. The advantage of registering a document is that any person who deals with the property would be bound by the rights that are created in earlier registered document.

### **Illustration**

A executes a mortgage on property X and gets it registered. Subsequently he sells property X to B, B is bound by the right of the mortgagee over the property X. Thus, whether B knows actually or not that there was a mortgage the fact that the earlier document was registered is a notice to B and B takes property,

subject to the rights of the mortgagee. Therefore, if a document of transfer relating to immoveable property is required by the law to be and has been effected by registered instrument, the persons who deal with the property subsequently are deemed in the eye of law as having knowledge of the such registered instrument from the date of its registration.

### **(iii) Notice**

Notice, may be actual or constructive. If a person knows about a fact, he has an actual notice. But, in certain circumstances law treats a man who ought to have known a fact even though he did not in fact know it. This is called constructive notice.

The equitable doctrine of notice is recognised in various Sections of this Act. For instance in Section 39 of the Act, where a transfer is made of property out of which a person has a right to receive maintenance, the transferee takes subject to that right if he had notice of it, but not otherwise. Similarly under Section 40 if A conveys to C property, which he had by a previous contract agreed to sell to B, then B can enforce the contract against C, if C had notice of it, but not otherwise. If C had notice of the prior contract, he purchases with knowledge that it was unconscionable of A to sell to him, and it is therefore, unconscionable of him to buy.

A person is deemed in the eye of law to have constructive notice of a fact when (i) but for willful abstention from an enquiry or search which he ought reasonably to have made; or (ii) gross negligence on his part, he would have known it. Constructive notice arises from an irrefutable presumption of notice. In law such a presumption will arise when (i) there is a willful abstention on the part of a person to make necessary enquiries regarding the existence of certain facts, or (ii) he showed gross negligence in the matter.

**The words “wilful abstention” suggest want of *bona fide* in respect of particular transaction (*Joshua v. Alliance Bank*, 22 Cal. 185). Thus, a person who refuses to receive a registered letter is, deemed to have constructive notice of its contents.**

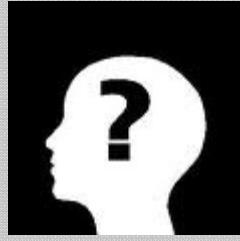
Similarly, if a person proposes to sell his property to X who, at the same time knows that rents due in respect of the property are paid by the tenants to a third person Y, X will be fixed with notice of the rights of Y (*Mernt v. Luck* (1902) 1 Ch. 429).

In so far as gross negligence is concerned, it does not mean a mere carelessness but means carelessness of such an aggravated nature as to indicate mental indifference to obvious risks. For example, if A buys property from B and does not care to ask whether any amount by way of municipal tax is due on that property and if the municipal corporation asks him to pay the arrears of tax, then B is responsible, and if he does not pay, then the arrears of tax may be made a charge on the property.

#### *Other Illustrations*

- (a) Where a purchaser was informed that the title deeds were in the possession of a bank for safe custody and yet failed to make any enquiry in the bank. It was held that he was guilty of gross negligence and must be deemed to have notice of the rights of the bank which has the custody of the title needs (*Imperial Bank of India v. Rai Gyand*, I A 283).
- (b) Where a person abstained from making further enquiries about the right of a person and did not cause a search, to be made in the office of the Sub-Registrar to ascertain if there was any encumbrance over the property, his omission must be held to be wilful or grossly negligent and he would be said to have notice of the prior encumbrances (*Rangappa Goundan v. Marapa Goundan*, AIR (1958) Madras 515).

The three Explanations to the definition of notice in Section 3, further mention certain circumstances wherein statutorily presumption of knowledge arises. These circumstances relate to the fact of registration (Explanation-I, Explanation-II) actual possession and notice to an agent (Explanation-III).

**Test your knowledge****State the following as "True" or "False"***According to general legal system of India, a minor cannot be a beneficiary under a contract.***Correct Answer: False****RESTRAINT ON TRANSFERS OR RULE AGAINST INALIENABILITY**

Section 10 of the Act says that when property is transferred, the transferee should not be restrained absolutely from alienating the property. One may give property to another subject to a condition, but the condition should not be one which absolutely prevents the transferee from alienating the property. Suppose, B gives property to A and his heirs adding a condition that if the property is alienated it should revert to B. This condition is invalid and the transferee can ignore such condition. The transfer takes effect and is valid, and the condition not to alienate the property is void.

**Examples of absolute restraint**

Suppose, A gives to B property worth only 2,000 rupees and adds a condition that B should sell property for Rs. 50,000 and not below that amount, this condition will at once become invalid for no one will buy the property which is only worth Rs. 2,000 for Rs. 50,000. Similarly, A gives to B property worth Rs. 50,000 and stipulates that if B wants to sell the property he should sell it to C only for Rs. 1,000. This again will operate as an absolute restraint. In *Rosher v. Rosher*, (1884) 26, Ch. D. 801, the testator gave his estate to his son and added a condition that if his son wanted to sell the property he should first give an option to the testator's wife who should be able to buy for £ 3,000. The market value of the property when the testator died was £ 15,000. It was held by the Court that the condition which compelled the son to sell the property for £ 3,000 was void. In *Trichinopoly Varthaga Sangum v. Shunmoga Sunderam*, (1939) Madras 954, there was a partition between a Hindu father and his five sons. The deed of partition provided that if any one of the sons wanted to sell his share, he should not sell it to a stranger but to one of his brothers who should have the option to buy for a sum not exceeding Rs. 1,000. It was held by the Court that the condition absolutely prevented the son from selling the property to any one for good value. In this case the market value of the property of the son was far greater than Rs. 1,000. Hence, the condition was declared invalid.

**Partial restraint valid**

Though absolute restraints are bad in law, partial restraints are valid. If there are conditions which restrain the transferee not to alienate the property outside the family, it has been held by the Courts that they are partial restraints. For example, whenever there are conditions in a family settlement whereby the members are not allowed to sell their shares to a stranger, such conditions are valid.

But it is not permissible to restrict the alienation to a particular time. Such a restriction is not partial but an absolute restraint and as such invalid.

**When absolute restraint valid?**

There are two exceptions to the rule that absolute restraints are void. Firstly, in the case of a lease, the lessor can impose a condition that the lessee shall not sublet the property or sell his leasehold interest. Such

conditions are valid. The reason why such an exception is made in the case of a lease is that the lessor may have confidence in the lessee but may not have the same confidence in some other person. So, if the lessor puts a condition restraining the lessee from transferring the property to someone, the condition is valid.

The second exception is made in respect of a woman who is not a Hindu, Buddhist or Muslim. In such a case, a condition to the effect that she shall not have power during her marriage to transfer the property is valid.

#### ***Restraint on enjoyment***

Section 11 of the Act also embodies a rule which is based on the principle that restraint on the enjoyment of the property is invalid. The section lays down that where land is transferred by one to another, the transferor should not impose conditions as to how and in what manner the transferee should enjoy the property.

#### ***Illustrations***

- (a) A sells his house to B and adds a condition that B only should reside in that house, the condition is invalid. This is subject to the exception that, if a person transfers a plot of land keeping another plot for himself, he can impose certain conditions which may interfere with the right of enjoyment of the transferee.
- (b) A has properties X and Y. He sells property Y to B and puts a condition that B should not construct on property Y more than one storey so that A's property X which he retains should have good light and free air.

Thus, it is clear in the above illustration that the condition which is imposed by A is for the benefit of another property which he retains. Such a condition is valid.

Section 12 also makes the transfer void if a property is transferred to any person adding a condition that if such person becomes insolvent he ceases to hold that property. Such a condition is not recognised as valid in law. Again, this is subject to the exception that if a landlord leases his property he can impose a condition on the lessee that if the lessee becomes insolvent the lease should come to an end.

#### ***TRANSFER FOR BENEFIT OF UNBORN PERSON***

Section 13 of the Transfer of Property Act lays down that where on a transfer of property, an interest therein is created for the benefit of a person not in existence at the date of transfer, subject to a prior interest created by the same transfer, the interest created for the benefit of such person shall not take effect unless it extends to the whole of the remaining interest of the transferor in the property. Thus if a property is given to an unborn person, two conditions should be satisfied:

- (i) it should be preceded by a life estate in favour of a living person, and
- (ii) it should comprise the whole of the remaining interest of the transferor so that there can be no further interest in favour of others.

#### ***Illustration***

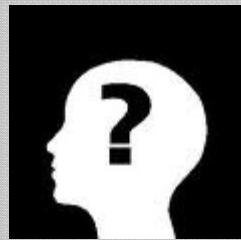
A transfers property of which he is the owner to B in trust for A and his intended wife successively for their lives, and after the death of the survivor, for the eldest son of the intended marriage for life, and after his death for A's second son. The interest so created for the benefit of the eldest son does not take effect, because it does not extend to the whole of A's remaining interest in the property.

**Test your knowledge****Choose the correct answer**

Which Section of the Transfer of Property Act provides that when a property is transferred, the transferee should not be restrained absolutely from alienating the property?

- (a) Section 2
- (b) Section 4
- (c) Section 8
- (d) Section 10

**Correct Answer: (d)**

**CONDITIONAL TRANSFER**

When an interest is created on the transfer of property but is made to depend on the fulfillment of a condition by the transferee, the transfer is known as a conditional transfer. Such a transfer may be subject to a condition precedent or a condition subsequent. If the interest is made to accrue on the fulfillment of a condition, the condition is said to be condition precedent. For instance, A agrees to sell his land to B if B marries C. This is a condition precedent. The condition precedent will be allowed to operate only if it is not hit by the provisions of Section 25 of the Act. Section 25 in the first place, says that, the condition must not be impossible to fulfil. For example, A lets a farm to B on condition that he shall walk a hundred miles in an hour. The lease is void. Secondly, the condition must not be forbidden by law. Thirdly, it should not be of such a nature that if permitted it would defeat the provisions of any law. For instance, A transfers Rs. 500 to B on condition that he shall murder C. The transfer is void. Fourthly, it should not be fraudulent. For example, X gives a false receipt to Y on behalf of his principal in consideration of transfer of land. The transfer would be void. Fifthly, the condition should not be such as to cause injury to the person or property of another. And lastly the condition should not be immoral or opposed to public policy. Thus, an agreement to give a son or daughter in adoption for a consideration is opposed to public policy as trafficking in children is forbidden by law.

If the condition is not hit by any of the above provisions, it is valid. Still the law does not insist on its literal fulfillment. It is sufficient if it is substantially complied with. Thus, where A transfers, Rs. 5,000 to B on condition that he shall marry with the consent of C, D and E. B marries with the consent of C and D only as E has died earlier. B is deemed to have fulfilled the condition.

A transfer may also be made subject to a contingency which may or may not occur. Thus, an interest may be created with the condition superadded that it shall cease to exist in case a specified uncertain event shall happen, or in case a specified uncertain event shall not happen.

This is known as condition subsequent. Condition subsequent is one which destroys or divests the rights upon the happening or non-happening of an event. For example, A transfers a farm to B for his life with a proviso that in case B cuts down a certain wood, the transfer shall cease to have any effect. B cuts down the wood. He loses his life interest in the farm. Similarly, if A transfers a farm to B provided that B shall not go to England within three years after the date of transfer, the interest in the farm shall cease. B does not go to England within the term prescribed. His interest in the farm ceases.

Now you will notice the distinction between condition precedent and condition subsequent. In condition precedent, the condition comes before the interest; whereas in condition subsequent, the interest is created before the condition. The one precedes the vesting of right and the other follows the vesting. In condition precedent, the vesting of right is delayed until the happening of an event. In condition subsequent, there is no postponement of vesting of right though it is to be destroyed or divested by reason of non-fulfilment of condition. There are certain situations where the law says that either the transfer will take effect on the fulfillment of a condition or will not take effect at all.

Again, if a transfer is made to defeat or delay the rights of a creditor, the transfer may be declared invalid by the creditor. In some cases, if property is transferred during the period when parties are litigating in a Court over a piece of property, then the transfer is not valid, or even if there is a transfer, it is subject to the rights that are created in the Court's decree. All these circumstances are given in the Transfer of Property Act e.g., doctrine of election, doctrine of fraudulent transfers and doctrine of *Lis pendens*.

## DOCTRINE OF ELECTION

Section 35 of the Transfer of Property Act deals with what is called doctrine of election. Suppose, a property is given to you and in the same deed of gift you are asked to transfer something belonging to you to another person. If you want to take the property you should transfer your property to someone else, otherwise you cannot take the property which is transferred to you by some one. Election may be defined as "the choosing between two rights where there is a clear intention that both were not intended to be enjoyed".

**The foundation of doctrine of election is that a person taking the benefit of an instrument must also bear the burden, and he must not take under and against the same instrument. It is, therefore, a branch of a general rule that no one may approbate and reprobate (*Copper v. Copper* (1874) H.L. 53). However doctrine of election could not be applied to deprive a person of his statutory right to appear invoking extraordinary jurisdiction of the Supreme Court under Article 136, (*PR Deshpande v. MB Haribatti* (1995 (2) Scale 804 SC).**

### Illustration

A transfers to you his paddy field and in the same deed of transfer asks you to transfer your house to C. Now, if you want to have the paddy field you must transfer your house to C, because the transferor is transferring to you his paddy field on the condition that you give your house to C.

Thus, either you take the paddy field and part with your house or do not take it at all. This is called the doctrine of election. You must elect either to take under the instrument, in which case you will have to fulfil the condition and bear the burden imposed upon you or you must elect against the instrument, in which case neither the benefit nor the burden will come to you. The doctrine is based on the principle that "a donee shall not be allowed to approbate and reprobate and that if he approbates, he shall do all in his power to confirm the instrument which he approbates" (*Cavendish v. Decre* 31 C.D. 466).

In case, the person upon whom benefit is conferred rejects it, the property which was attempted to be transferred to him will revert to the transferor and it is he who will compensate the disappointed person. If the transferor dies before the person upon whom the benefit is conferred and he rejects the transfer, then the representatives of the transferor will have to satisfy the disappointed person out of the property which was the subject of transfer.

### Explanation of the above principle

A transfers his property worth Rs. 1,000 and by the same instrument asks B to transfer his property worth Rs. 500 to C. Here, if B does not accept, he will not take A's property and the property will revert to A. If A is

alive, it is for him to give some property to C. But if A dies before B has made his election then the heirs of A have to compensate C from A's property to the extent of Rs. 500. (You will note that B's property worth Rs. 500 was intended by A to be transferred to C).

The question of Election arises only when a transfer is made by the same document. If the transferor makes a gift of property by one deed and by another asks the donee to part with his own property then there is no question of election.

### **Illustration**

A transfers his land to B by a document. A by another document transfers B's property to C. In this case B can retain the property given to him and refuse to transfer his property to C as the two transfers do not form part of the same document.

Further, the doctrine of election is applicable if the benefit is given directly. A person taking no benefit directly under a transaction but deriving a benefit under it indirectly need not elect.

### **Illustration**

A transfers his property to B's son and by the same instrument transfer B's property to C. In this case B need not to elect and can keep his property. His son can have his gift.

There is, however, an exception to the doctrine of election. That is, if the transferor gives two benefits to a person and one particular benefit is in lieu of an item of property belonging to that person which the transferor has asked to transfer to a third-party then if the person elects to retain his property, he can retain the other benefit.

### **Illustration**

Under A's marriage settlement, his wife is entitled, if she survives him to the enjoyment of the estate of Sultanpur during her life. A by his will bequeaths to his wife an annuity of Rs. 200 p.m. during her life, in lieu of her interest in the estate of Sultanpur, which estates he bequeaths to his son. A also gives his wife a legacy of Rs. 1,000. After the death of A, his widow elects to take what she is entitled to take under the marriage settlement (i.e., the enjoyment of estate of Sultanpur). In this case, the wife has to forfeit the claim of Rs. 200 which her husband has given to her. But she can claim other benefit i.e., Rs. 1,000.

Election may be express or implied by conduct.

### **Illustration**

A transfers to B an estate to which C is entitled, and as part of the same transaction gives C a coal mine. C takes possession of the mine and exhausts it. He has thereby confirmed the transfer.

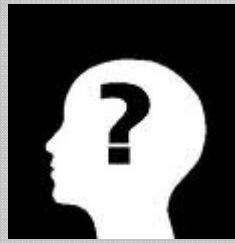
In case of disability, the condition shall be postponed until the disability ceases, or until the election is made by some competent authority.

### **Test your knowledge**

**State the following as "True" or "False"**

*If the interest is made to accrue on the fulfilment of a condition, the condition is said to be condition precedent.*

**Correct Answer: True**



## TRANSFER BY OSTENSIBLE OWNER OR DOCTRINE OF HOLDING OUT

Where, with the consent, express or implied, of the persons interested in immoveable property, a person is the ostensible owner of such property and transfers the same for consideration, the transfer shall not be voidable on the ground that the transferor was not authorised to make it, provided that the transferee, after taking reasonable care to ascertain that the transferor had power to make the transfer, has acted in good faith. (Section 41)

The following conditions are necessary for the application of Section 41:

- (i) the transferor is the ostensible owner;
- (ii) he is so by the consent, express or implied, of the real owner;
- (iii) the transfer is for consideration, and
- (iv) the transferee has acted in good faith taking reasonable care to ascertain that the transferor had power to transfer.

If any one of these elements is absent, the transferee is not entitled to the protection of this section.

This Section is a statutory application of the law of estoppel. The section makes an exception to the rule that a person cannot confer a better title than he has. An ostensible owner is one who has all the *indicia* of ownership without being the real owner.

### Illustrations

- (a) A made a gift of property to B but continued in possession of the gifted property. He purported to exercise a power of revocation and then transferred the property to the defendant. The gift, however, was not revocable as it was an unconditional gift. B seeks to recover possession from the defendant. The defendant invoked protection under Section 41.

In the given example, the donor is not an 'ostensible owner' holding the property with the consent of the real owner. The defendant cannot, therefore, invoke the protection of Section 41.

- (b) The manager of a joint Hindu family consisting of some minor members alienated the ancestral house to P without any necessity and the alienee transferred it to the defendants. The minors challenged the alienation. The defendants sought protection under Section 41.

Here Section 41 has no application for "P was not the ostensible owner of the ancestral family house with the consent, express or, implied, of the persons interested in the said ancestral house in as much as the plaintiff, who had an interest in the said house, did not and could not by reason of the disability of infancy give their consent".

## DOCTRINE OF FEEDING THE GRANT BY ESTOPPEL

Where, a person fraudulently or erroneously represents that he is authorised to transfer certain immoveable property and professes to transfer such property for consideration, such transfer shall, at the option of the transferee, operate on any interest which the transferor may acquire in such property at any time during which the contract of transfer subsists. (Section 43)

Nothing in this Section shall impair the right of transferees in good faith for consideration without notice of the existence of the said option.

**Essentials:** In order to invoke this section, the transferee must prove that:

1. there was a representation, fraudulent or erroneous;
2. it was to the effect that the transferor is entitled to transfer the immoveable property;

3. the transferor is found to have subsequently acquired the interest which he professed to transfer;
4. the transfer of property was for consideration;
5. the transferee has not rescinded the contract;
6. the transferee acted in good-faith for consideration and without notice of the rights under the prior transfer.

### **Illustration**

A, a Hindu, who has separated from his father B, sells to C three fields, X, Y and Z, representing that A is authorised to transfer the same. Of these fields, Z does not belong to A, it having been retained by B on the partition, but on B's dying, A as heir obtains Z. C, not having rescinded the contract of sale may require A to deliver Z to him. Thus, where a grantor has purported to grant an interest in land which he did not at that time possess, but subsequently acquires, the benefit of his subsequent acquisition goes automatically to the earlier grantee or as it usually expressed, feeds the estoppel.

### **DOCTRINE OF FRAUDULENT TRANSFER**

Where a person transfers his property so that his creditors shall not have anything out of the property, the transfer is called a fraudulent transfer. A debtor in order to defeat or delay the rights of a creditor, may transfer his property to some person, who may be his relative or a friend. The law does not allow this. Section 53 embodies the principle. It states :

"Every transfer of immoveable property made with intent to defeat or delay the creditors of the transferor shall be voidable at the option of any creditor so defeated or delayed."

Thus, where an owner of the property contracts a debt and then transfers his property to someone so that the creditor cannot proceed against the property to realise his debt, such a transfer is voidable at the option of the creditor. The transfer is valid so long as the creditor does not challenge it in a Court of law and gets a declaration that the transfer is invalid. A suit instituted by a creditor to avoid a transfer on the ground that it has been made with intent to defeat or delay the creditors of the transfer or shall be instituted on behalf of, or for the benefit of all the creditors. Once the creditor sues the debtor and says that the debtor has the intention to deceive him, the transfer can be declared invalid by the Court. The creditor has to satisfy the Court that there was an intention on the part of the debtor to defeat his rights. If he does not prove this, then the creditor will fail and the transfer is valid. The question arises as to when we can say that the transferor has the necessary intention to defeat the claim of the creditor. This can be gathered from the surrounding circumstances. Suppose a man takes a loan from the creditor. He does not pay the loan. Then the creditor sues him in a Court to get back his debt. On seeing this the debtor transfers his property to a friend of his or some other person who simply holds the property on behalf of the transferor. Again, the debtor may make a gift of his property to his wife or sell it to a friend who will afterwards retransfer the same to the transferor. Under these circumstances, we can easily say that the debtor's intention was to prevent the creditor from taking the property by a suit in the Court and to realise his debt.

But suppose the debtor has several creditors and he transfers his property to one of his creditors in satisfaction of his whole debt to him. Is this also a fraudulent transfer? The answer is No. For a mere preference of one creditor over the others is not fraudulent under the Section, even if the whole property is so transferred and nothing is left for the other creditors. But the other creditors may file a petition in the Court within three months of the transfer praying that the debtor be declared insolvent. If the debtor is adjudicated an insolvent, their interest will be protected and the transfer will be declared as fraudulent preference. The transfer will be set aside and the property will be distributed among all the creditors.

However, under Section 53(2) the rights of a transferee in good-faith and for consideration are protected. It says nothing shall affect or impair the rights of a transferee in good-faith and for consideration.

## DOCTRINE OF PART-PERFORMANCE

Lastly, we may also discuss briefly the doctrine of part-performance which is embodied in Section 53A of the Transfer of Property Act.

A contract for the sale of land has been entered into between A and B. The transferee has paid the price entering into possession and is willing to carry out his contractual obligations. As registration has not been effected A, the transferor, seeks to evict B from the land. Can he do so? No, B will not be allowed to suffer simply because the formality of registration has not been through. The legislature grants some relief to such a transferee under Section 53A, which embodies the doctrine of part-performance.



*The rule did not exist on the statute book before 1929. Section 53A, was inserted by an amendment to the Act in 1929. Followings are the essential conditions for the operation of the doctrine of part-performance according to Section 53A.*

1. *There must be a contract to transfer immoveable property.*
2. *It must be for consideration.*
3. *The contract should be in writing and signed by the transferor himself or on his behalf.*
4. *The terms necessary to constitute the transfer must be ascertainable with reasonable certainty from the contract itself.*
5. *The transferee should have taken the possession of the property in part performance of the contract. In case he is already in possession, he must have continued in possession in part performance of the contract and must have done something in furtherance of the contract.*
6. *The transferee must have fulfilled or ready to fulfill his part of the obligation under the contract.*

If all the abovementioned conditions are satisfied, then, the transferor and the persons claiming under him are debarred from exercising any right in relation to the property other than the rights expressly provided by the terms of the contract notwithstanding the fact that the instrument of transfer has not been registered or complete in the manner prescribed therefor by the law for time being in force. It should be noted that Section 53A does not confer any positive right on the transferee. It only prohibits exercise of the right of ownership in relation to the property in order to evict the transferee from the property because legal requirements have not been satisfied.

However, the doctrine of part-performance will not affect the right of a subsequent transferee for consideration without notice of the earlier contract and of its being partly performed.



*The right conferred by this section is a right only available to a defendant to protect his possession. This section does not create a title on the defendant. It merely operates as a bar to the plaintiff asserting his title. It is limited to cases where the transferee had taken possession, and against whom the transferor is debarred from enforcing any right other than that expressly provided by the contract. The section imposes a bar on the transferor. When the conditions mentioned in the sections are fulfilled, it debars him from enforcing against the transferee any right or interest expressly provided by the contract. So far as the transferee is concerned, the section confers a right on him to the extent it imposes a bar on the transferor (Delhi Motor Co. v. Basurkas, (1968) SCR 720).*

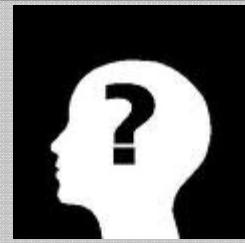
The English rules as to what acts constitute part-performance have been generally followed in India. These rules are as follows:

- (1) An act of part-performance must be an act done in performance of the contract. An act introductory to and previous to the agreement, cannot therefore, be act of part-performance.
- (2) The acts relied upon must be unequivocally and referable to no other contract than that alleged.
- (3) An act of part-performance must be the act of the party seeking to avail himself of the equity.

### ***Test your knowledge***

***State the following as "True" or "False"***

*In a fraudulent transfer a person transfers his/her property so that his/her creditors shall not have anything out of the property.*



***Correct Answer: True***

## **PROPERTIES WHICH CANNOT BE TRANSFERRED**

Section 6 of this Act contains some exceptions to the general rule that property of any kind may be transferred. Consequently, the following properties cannot be transferred, namely:

- (a) the chance of an heir apparent succeeding to an estate, the chance of a relation obtaining a legacy on the death of a kinsman or any other mere possibility of a like nature cannot be transferred.
- (b) A mere right of re-entry for breach of a condition subsequent cannot be transferred to any one except the owner of the property affected thereby.
- (c) An easement cannot be transferred apart from the dominant heritage.
- (d) An interest in property restricted in its enjoyment to the owner personally cannot be transferred by him.
- (e) A right to future maintenance in whatsoever manner arising, secured or determined, cannot be transferred.
- (f) A mere right to sue cannot be transferred.
- (g) A public office cannot be transferred nor can the salary of a public officer, whether before or after it has become payable.
- (h) Stipends allowed to military, naval, air force and civil pensioners of the Government and political pensions cannot be transferred.

### ***(a) Chance of an heir apparent or 'Spes Successionis'***

In this clause possibilities referred are bare or naked possibilities and not coupled with an interest such as contingent remainders or future interest-also known as right of *spes successionis* which cannot be the subject to transfer.

When a person is the owner of property, the property is in existence and it is in his possession. This he may transfer. But if property is neither in existence nor is the person the owner of the property then it cannot be transferred. For example, if a person is intending to buy certain property but, he has no interest in that property, he cannot transfer it unless the property comes to his hands, i.e., unless he becomes the owner of

the property after buying it. But if a person obtains certain consideration and agrees to sell the property of which he is not the owner, then on becoming the actual owner of the property he has to transfer the property as there was a contract between him and the person who has agreed to buy the property. This transfer operates on a contract to be performed when the property comes into the hands of the person who has agreed to transfer. But where a person wants to make a gift of the property which is to come in his hands in future, he cannot transfer it because a gift is voluntary transfer without any consideration. Thus a gift of future property is void. Similarly, the chance of a heir apparent succeeding to the estate of a deceased person cannot be transferred. Suppose A is the owner of the property and B is his son. B is the heir of A. During the life time of his father A, B has only a hope expectancy that he will inherit the property of his father. This type of property which B hopes to get after the death of the father cannot be transferred, during the life time of A.

#### **Illustrations:**

- (a) Suppose A, a Hindu who has separate property, dies leaving a widow W and a brother L, L's succession to the property is dependent upon two factors, viz., (i) his surviving the widow, W, and (ii) W leaving the property intact. L has only a bare chance of succession to the property left by A. This is *spes successionis*, and therefore, cannot be transferred (*Amrit Narayana v. Gyan Singh*, (1918) 45 Cal. 690).
- (b) A transfers to B for valuable consideration his reversionary interest in a property. When A succeeds to the property, B sues him for possession of the same. B will not succeed as the reversionary interest is a *spes successionis* and non-transferable. So the transfer is void and B's suit for possession fails.

#### **(b) Right of re-entry**

The right which the lessor has against the lessee for breach of an express condition which provides that on its breach the lessor may re-enter is called the right of re-entry. For instance, if A leases his property to B and adds a condition that if B sub-lets the leased land, A will have the right to re-enter, i.e., the lease will terminate if the lessee breaks the condition by subletting to a third person. Thus, right of re-entry being a right for the personal benefit of any party cannot exist for the benefit of a person who has no personal interest in the land. For example, A grants his land by way of lease to B, a limited liability company on condition that the land should revert to A from B if the company goes into liquidation. This is a mere right in favour of A and this right A cannot transfer to anyone as this is a personal right which can be exercised by A only. But if A transfers the whole of his interest in the land including the right of re-entry to C, there the right to re-entry is a legal incident of property and can be validly transferred along with the property.

#### **(c) Transfer of easement**

An easement is a right enjoyed by the owner of land over the land of another: such as, right of way, right of light, right of support, right to a flow of air or water. Section 4 of the Easements Act defines an easement as a right which the owner or occupier of certain land possesses as such for the beneficial enjoyment of the land, to do and continue to do something or to prevent and to continue to prevent something being done in or upon or in respect of certain other and not his own land. An easement includes a right to enjoy a profit out of the land of another. An easement exists for the accommodation and better enjoyment of the land to which it is annexed. The land owned by the possessor of the land is known as *dominant tenement* and the land over which the right is enjoyed is known as the *servient tenement*. As an easement confers no proprietary right on its owner, it cannot be transferred apart from the land itself. For example, the right of certain villagers to bathe in another's tank cannot be transferred. Similarly if A, the owner of a house X, has a right of way over an adjoining plot of land belonging to B, he cannot transfer this right of way to C. But if he transfers the house itself to C, the easement is also transferred to C.

It may be noted, however, that the prohibition is only with regard to transfer of an existing easement. The law

does not prohibit the grant or creation of new easement (*Bhagwan Sahai v. Narsing*. (1909) 31 ALL. 612; *Satyanarayana v. Lakshamaya* 5 H.L.J. 56 or the extension of an easement by release in favour of the owner of servient tenement).

**(d) Restricted interest or personal interest**

An interest restricted in enjoyment to the owner personally is by its very nature not transferable unless the restriction is void under Section 10. Examples of such restricted interest or property are the following:

- (i) The right of pre-emption given under the Mohammedan Law.
- (ii) The office of a Shebait of a Temple or mohunt of a mutt or mutuwalli of a wakf.
- (iii) Emoluments attached to a priestly office.
- (iv) Service tenures.

**(e) Right to future maintenance**

This again is a personal right in the property which the law says that it cannot be transferred. The right of a Hindu widow to maintenance is a personal right which cannot be transferred. Under the law the arrears of past maintenance can be transferred, but not the right to future maintenance.

**(f) Mere right to sue and actionable claim**

A 'mere right to sue' apart from the interest from which such right accrues cannot be assigned. The 'right to sue' is a personal right annexed to the ownership of property and cannot be *severed*, from it. It is based on the principle of public policy to prevent multiplicity of suits; the object is mainly to prevent the abuse resulting from trafficking in litigation.

The use of the word "mere" is significant. The question in every case is whether the subject-matter of transfer is property with an incidental remedy for its recovery or is a 'mere' right to 'sue'. Where property is transferred along with a right to recover damages or compensation in respect of the property, the assignment is not hit by clause (4) of Section 6 of the T.P. Act.

A mere right to sue cannot be transferred. The right refers to a right to damages arising both out of contracts as well as torts. For example, A commits an assault on B, B can file a suit to obtain damages; but B cannot assign the right to C and allow him to obtain damages. In contract also, the rule is the same. If A breaks a contract which he has entered into with B, B can bring action for damages, but B cannot transfer this right to C to recover damages.

There is clear distinction between an actionable claim and a mere right to sue. An actionable claim is property and the assignee has a right to sue to enforce the claim.

As already noted a right to recover an unascertained amount of damages resulting from breach of contract or tort is a mere right to sue. If, however, one has a right to recover an ascertained and definite debt, he may transfer it because it is an actionable claim. Thus, suppose A is indebted to B for Rs. 2,000 and B transfers the right to recover the debt of C, the transfer is void. A beneficial interest in specific moveable property is also an actionable claim. It has been held that the right to claim the benefit of an executory contract constitutes a beneficial interest in moveable property (*Jaffer Meher Ali v. Budge Budge Jute Mills*, (1900) 33 Cal. 702).

After breach of a contract for the sale of goods nothing is left but a right to sue for damages which cannot be transferred. But before breach the benefit of an executing contract for the sale of goods may generally be transferred and the buyer has the right to sue for the goods.

**(g) Transfer of public office and salaries, stipends, etc.**

It is against public policy for a public officer to transfer the salary of his office, for the salary is given for the purpose of upholding its dignity and the proper performance of its duties. Civil and military pensions are not transferable. A pension retains its character as long as it is unpaid and is in the hands of Government, but as soon as it is paid to the pensioner or his legal representatives, it can be transferred. Since these allowances, pensions and stipends are given on personal basis, the law does not allow these types of property to be transferred.

**RULE AGAINST PERPETUITY**

Section 14 of the Act provides that no transfer of property can operate to create an interest which is to take effect after the life time of one or more persons living at the date of such transfer, and the minority of some person who shall be in existence at the expiration for that period, and to whom, if he attains full age, the interest created is to belong.

The rule against perpetuity is based on the general principle that the liberty of alienation shall not be exercised to its own destruction and that all contrivances shall be void which tend to create a perpetuity or place property forever out of the reach of the exercise of the power of alienation. Perpetuity has been described as "exemptions from intermission or ceasing". This has been said to be "odious in law, destructive to the commonwealth, and an impediment to commerce, but preventing the wholesome circulation of property".

A perpetuity in the primary sense of the word, "is a disposition which makes property inalienable for an indefinite period" (Jarman on Wills, 8th ed., vol. 1, P. 284). Section 14 of the Act adopted with certain modifications the English rule against perpetuities which is enunciated by Jarman as "Subject to the exceptions to be presently mentioned, no Contingent or executory interest in property can be validity created, unless it must necessarily vest within the maximum period of one or more lives in being and twenty-one years afterwards". Section 14 of the Act fixes the perpetuity period as: Life (or Lives) living at the time of transfer and actual minority of the then unborn ultimate transferee.

Any number of successive estates can be created between the transferees who are living persons e.g. A transfer may be made to A for life and then to B for life and then to C for life and so on, provided that A, B and C are all living persons at the date of the transfer. But if the ultimate beneficiary is some one who is not in existence at the date of the transfer, the whole residue of the estate should be transferred to him. If he is born before the termination of the last prior estate, he takes a vested interest at birth and takes possession on the termination of the last prior estate but if he is not born till the termination of the last prior estate, the transfer to him fails.

Further, the rule is not that vested interest is created at the birth of the beneficiary but that vested interest cannot be delayed in any case beyond his minority. Therefore, the rule against perpetuity is that the minority of the ultimate beneficiary is the latest period at which an estate can be made to vest.

In India minority terminates at the end of 18 years.

The rule against perpetuities applies to both moveable and immoveable property.

Thus, the rule against perpetuity contains two propositions, i.e.:

- (1) No transfer is valid after the life-time of one or more persons living at the date of such transfer.  
Transfer can remain in effect only during the life time of an existing person.
- (2) Transfer can be extended to a person who is not in existence but if he is in existence at the time of termination of the period of last transfer. The moment the person is born he shall have contingent interest and after minority i.e. after the age of 18 years, he shall have vested interest. Barring these two conditions, a restriction on alienation of a property is void.

The rule against perpetuities is also called the rule against remoteness because it is directed against limitations which are too remote and are expressed to take effect beyond the maximum period permitted by law.

However, Section 18 provides an exception to the above rule of perpetuity, where the transfer of property is for the benefit of the public in the advancement of religion, knowledge, commerce, health, safety, or any other object beneficial to mankind.

#### *Effect of a transfer on failure of prior interest*

Further, where by reason of any rules or the rules contained in Sections 13 and 14, interest created for the benefit of a person or class of persons fails in regard to such person or the whole of such class, any interest created in the same transaction and intended to take effect or upon failure of such prior interests also fail (Section 16). For example, property is transferred to A for life then to his unborn son B for life and then to C, who is living at the date of transfer, absolutely. Here B is given only a life interest. So the transfer to B is invalid under Section 13. The subsequent transfer to C absolutely is also invalid, because according to Section 16, if a prior transfer fails, the subsequent transfer will also fail.

No transfer of property can operate to create an interest which is to take effect after the life time of one or more persons living at date on such transfer, and the minority of some person who shall be in existence on the expiration of that period, to whom, if he attains full age, the interest created is to belong.

The policy of the law has been to prevent property being tied up for ever. The vesting cannot be postponed beyond the life time of any person living at the date of transfer. For example, if an estate is given to a living person A for life and then to the unborn son of A, the son of A must be in existence on or before the date of the expiry of the life estate in favour of A. The vesting of absolute interest in favour of an unborn person may be postponed until he attains majority. For example, an estate may be transferred to A, living person, and after his death to his unborn son when he attains the age of 18. Such transfer would not be violative of the rule against perpetuity.

### ACCUMULATION OF INCOME

Section 17 does not allow accumulation of income from the land for an unlimited period without the income-being enjoyed by owner of the property. The law allows accumulation of income for a certain period only. The period for which such accumulation is valid is :

- (a) the life of the transferor, or
- (b) eighteen years from the date of transfer.

Any direction to accumulate the income beyond the period mentioned above is void except where it is for:

- (i) the payment of the debts of the transferor or any other person taking any interest under the transferor,
- (ii) portions for children or any other person taking any interest in the property under the transfer, and
- (iii) for the preservation and maintenance of the property transferred.

#### *Test your knowledge*

***State the following as "True" or "False"***

*A public office cannot be transferred nor can the salary of a public officer.*

***Correct Answer: True***



## DOCTRINE OF *LIS PENDENS*

*Lis* means dispute, *Lis pendens* means a pending suit, action, petition or the like. Section 52 of the T.P. Act incorporates the doctrine of *Lis pendens*. It states that during the pendency of a suit in a Court of Law, property which is subject to a litigation cannot be transferred. When we say that property cannot be transferred what we mean in this context is that property may be transferred but this transfer is subject to the rights that are created by a Court's decree. For example, A and B are litigating in a Court of law over property X and during the pendency of the suit A transfers the property X to C. The suit ends in B's favour. Here C who obtained the property during the time of litigation cannot claim the property. He is bound by the decree of the Court wherein B has been given the property.

Section 52 lays down the Indian rule of *Lis pendens* being the legislative expression of the Maxim- “*ut lite pendente nihil innovetur*” ‘During litigation nothing new should be introduced’.

### Essentials

In order to constitute a *Lis pendens*, the following elements must be present:

1. There must be a suit or proceeding in a Court of competent jurisdiction.
2. The suit or proceeding must not be collusive.
3. The litigation must be one in which right to immoveable property is directly and specifically in question.
4. There must be transfer of or otherwise dealing with the property in dispute by any party to the litigation.
5. Such transfer must effect the rights of the other party that may ultimately accrue under the terms of the decree or order.

The rule is based on the doctrine of expediency i.e., the necessity for final adjudication. A plea of *lis pendens* will be allowed to be raised even though the point is not taken in the pleadings or raised as an issue.

When an application to sue in *forma pauperis* is admitted, the suit is pending from the time of presentation of the application to the Court but not if it is rejected.

A suit in foreign Court cannot operate as *lis pendens*. The doctrine of *lis pendens* does not apply to moveables. It is the essence of the rule that a right to immoveable property is directly and specifically in question in the suit. The doctrine is not applicable in favour of a third-party.

### Effect

If the parties to the litigation, are completely prevented from transferring the property in litigation, it would cause unnecessary delay and hardship, as they would have to wait till the final disposal of the case. So, Section 53 creates a limitation over the transfer by making it subject to the result of the litigation. The effect of this doctrine is not to invalidate or avoid the transfer, or to prevent the vesting of title in the transfer, but to make it subject to the decision of the case, and the rule would operate even if the transferee *pendente lite* had no notice of the pending suit or proceeding at the time of the transfer.

## PROVISIONS RELATING TO SPECIFIC TRANSFERS

The Act expressly provides for special types of transfers such as sale, exchange, gift, mortgage and lease.

These are as follows:

In a sale, exchange and gift, there is a transfer of the ownership of property but mortgage is a transfer of an interest in specific immoveable property and lease is a transfer of the right to enjoy immoveable property.

**1. Sale**

*Under Section 54 of the T.P. Act, "sale" has been defined as a transfer of ownership in exchange for a price paid or promised or part paid and part-promised.*

**Essentials**

- (a) The seller must be a person competent to transfer. The buyer must be any person who is not disqualified to be the transferee under Section 6(h)(3).
- (b) The subject matter is transferable property.
- (c) There is a transfer of ownership. This feature distinguishes a sale from mortgage, lease etc., where there is no such transfer of ownership.
- (d) It must be an exchange for a price paid or promised or part paid and part promised.
- (e) There must be present a money consideration. If the consideration is not money but some other valuable consideration it may be an exchange or barter but not a sale.

**Mode of transfer by sale**

Sale of an immoveable property can be effected,

- (a) Where such property is tangible (i) by a registered instrument if it is of the value of Rs. 100 and upwards, and (ii) by a registered instrument or by delivery of property when it is less than Rs. 100 in value, and
- (b) Where the property is tangible or a reversion, only by a registered instrument.

**Contract for sale**

A contract for the sale of immoveable property differs from a contract for the sale of goods in that the Court will grant specific performance of it unless special reasons to the contrary are shown.

The rights and liabilities of a seller and buyer are dealt with in Section 55 of the Transfer of Property Act.

**2. Exchange**

Sections 118 to 121 of the Transfer of Property Act, 1882 deal with "Exchanges".



*When two persons mutually transfer the ownership of one thing for the ownership of another, neither thing or both things being money only, the transaction is called an "exchange".*

**Essentials**

- (i) The person making the exchange must be competent to contract.
- (ii) There must be mutual consent.
- (iii) There is a mutual transfer of ownership though things and interests may not be identical.
- (iv) Neither party must have paid money only.

This Section applies to both moveable and immoveable property.

### Mode of exchange

A transfer of property in completion of an exchange can be made only in the manner provided for the transfer of such property by sale.

### 3. Gift

The provisions relating to "Gifts" have been stipulated under Sections 122 to 128 of the Act.

Section 122 of the Transfer of Property Act defines "gift" as follows:

 "Gift" is the transfer of certain existing moveable or immoveable property made voluntarily and without consideration by one person called the donor, to another called the donee and accepted by or on behalf of the donee.

Such acceptance must be made during the life time of the donor and while he is still capable of giving. If the donee dies before acceptance, the gift is void.

### Essentials

1. There must be a transfer of ownership.
2. The subject matter of gift must be a certain existing moveable or immoveable property.
3. The transfer must be made voluntarily.
4. It must be done without consideration.
5. There must be acceptance by or on behalf of the donee, and such acceptance must be made during the lifetime of the donor and while he is capable of giving.

There are two parties to the gift: donor and donee. The donor must be a person competent to transfer; whereas the donee may be any person. The gift can be made to any one, to an incompetent person or even to a juridical person. The essence of a gift is that it is a gratuitous transfer.

According to Section 123, a gift of immoveable property must be made by a registered instrument signed by or on behalf of the donor and attested by at least two witnesses. A gift of moveable property may be made by a registered instrument or by delivery of property. Where the donee is already in possession of the moveable property, as no future delivery is possible, the donor may make a declaration of the gift in his favour. For example, where a piece of furniture or a television set belonging to the donor is lying with a friend of his, the donor may simply declare that he makes a gift of the furniture or the television set and the gift is complete. The declaration must be clear and the donee must accept the gift.

A gift of immoveable property, as said above, must be effected by registration. Where a gift in favour of someone is registered but it is not accepted by the donee, the gift is incomplete. Suppose, a document is executed by the donor who makes a gift of immoveable property and the deeds are delivered to donee, and the donee accepts the gifts but the document is not registered. Will the gift be valid? It has been held by the Courts that the gift is valid. While registration is a necessary formality for the enforcement of a gift of immoveable property, it does not suspend the gift until registration actually takes place. The donee in such a case can ask the donor to complete the gift by registration. Thus, the most essential thing for the validity of a gift is its acceptance. If the gift is accepted but not registered it is a valid gift. **The Privy Council in Kalyan Sundram v. Kumarappa, A.I.R. 1925 P.C. 42, decided that after acceptance of the deed of gift and before registration, the donor cannot revoke the gift. The gift which is accepted by the donee, will take effect from the date of the execution of the document by the donor, even though it is registered at a later date.**

If the deed of gift is executed but never communicated to the intended donee and remains in the possession of the donor undelivered, it cannot be compulsorily registered at the instance of the donee. The reason is that

the donee did not accept the gift, the donor can at any time before such acceptance revoke the gift. But once a gift is accepted by the donee, the donor cannot revoke it. A gift may, however, be revoked if it is brought about by a fraud or misrepresentation or undue influence.

The other essential characteristic of a gift is that it cannot be revoked at the will and pleasure of the grantor. A revocable gift is one which may be revoked by the donor at any time. Its revocation would depend upon the mere will or pleasure of the donor. Such a gift is void. But on the other hand, if the condition is one which does not depend on the will or pleasure of the donor, the gift can be revoked on the happening of such condition.

### Illustrations

- (a) A gives a field to B, reserving to himself, with B's assent, the rights to take back the field in case B and his descendants die before A, B dies without descendants during A's lifetime. A may take back the field.
- (b) A gives a lakh of rupees to B, reserving to himself with B's assent the right to take back at leisure Rs. 10,000 out of one lakh. The gift holds goods as to Rs. 90,000 but is void as to Rs. 10,000 which continues to belong to A.

A gift which comes into existence on the fulfilment of a condition, that is to say, a gift which is subject to a condition precedent is also valid. A condition precedent, as already explained in this study dealing with vested interest and contingent interest, is one which must be fulfilled before the transfer takes effect. But the condition attached to the gift should not be illegal or immoral. For instance, a gift to A on condition that he murders B is not valid.

A gift comprising both of existing property and future property is void as to the latter. For example, A makes a gift of his house and also makes a gift of the additions that he is likely to make in future. Here the gift of the house is valid but the gift of the additions that are yet to be made is invalid.

*Onerous gift:* Lastly reference may also be made to what is known as an onerous gift. It may be that several things are transferred as a gift by single transaction. Whereas some of them are really beneficial the others convey burdensome obligations. The result is that the benefit which it confers is more than counter balanced by the burden it places. For instance, A makes a gift of shares in the companies X and Y. X is prosperous but heavy calls are expected in respect of shares in Y company. The gift is onerous. The rule as laid down in Section 127 is that the donee takes nothing by the gift unless he accepts it fully. Where the gift is in the form of two or more independent transfers to the same person of several things, the donee is at liberty to accept one of them and refuse the other.

The rules pertaining to gifts in the Transfer of Property Act do not apply to the gifts by Mohammedans. If a gift is made by a Mohammedan, its validity has to be judged according to Muslim law and not according to the Transfer of Property Act.

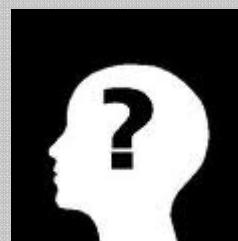
### Test your knowledge

**State whether the following statement is “True” or “False”**

*If the donee dies before acceptance, the gift is void.*

- True
- False

**Correct Answer: True**



#### 4. Leases



(i) *Meaning and nature of lease:* According to Section 105, a "lease" of immoveable property is a transfer of a right to enjoy property. Since it is a transfer to enjoy and use the property, possession is always given to the transferee. The lease of immoveable property must be made for a certain period. For example, you may give a lease of property for a definite number of years, or for life, or even permanently.

#### Essentials

The essentials of a lease are:

- (1) It is a transfer of a right to enjoy immoveable property;
- (2) Such transfer is for a certain time or perpetuity;
- (3) It is made for consideration which is either premium or rent or both;
- (4) The transfer must be accepted by the transferee.

The transferor is called the lessor, the transferee is called the lessee, the price is called premium and the money, share, service or any other thing of value to be so rendered is called the rent.

The parties to the lease (i.e. lessor and lessee), must be competent to make and to take the lease respectively.

(ii) *Lease and licence:* A lease should be distinguished from a licence. A licence is a right to do or continue to do in or upon the immoveable property of the grantor, something which would, in the absence of such a right, be unlawful.

A licence does not transfer any interest in the property and the licensee has no right to possession. A licence can be revoked by the grantor at any time, whereas a lease cannot be revoked. If, I sell the fruits of my garden to you, you are given permission or licence to enter my garden and take away the fruits. A lease involves a transfer of interest followed by possession of the property for a specified period. The real test is the intention of the parties.

**If the document creates an interest in the property, it is a lease but if it only permits another to make use of the property of which the legal possession continues with the owner, it is a licence because it does not create any interest in that property (*Associated Hotel of India v. R.N. Kapoor, A.I.R. (1956 S.C. 1962*).**

The question is not of words but of substance and the label which the parties choose to put upon the transaction though relevant is not decisive.

(iii) *Formalities:* According to Section 107, a lease from year to year or for any term exceeding one year can be made only by a registered document. If a lease is for a term below one year, it can be made by an oral agreement. If a lease is created by oral agreement, it must be accompanied by delivery of possession. If the lease is for a year or more, it must be effected by a registered document. If after the registration, the lessor does not give possession, the lessee can sue for possession.

(iv) *Types of tenancies:* Following are the various types of tenancies:

- (a) *Tenancy from year to year:* A tenancy from year to year may be made by a grant of land from year to year. If the tenancy is for a year to start with but after the expiration of one year the lessee continues to be in possession and pays the rent to the landlord, the tenancy is regarded as a year-

to-year tenancy. If, in case of a tenancy for a period more than a year the landlord wants to terminate or end the lease, he has to give a six-month's notice to the lessee to quit. In case of a tenancy from month to month, a fifteen days notice to quit is necessary. The monthly tenancy may be created either by contract or may be presumed from the nature of the tenancy to be one, from month to month.

- (b) *Tenancy-at-will:* Tenancy-at-will is a tenancy recognised by law. This comes into existence where a tenant holds over with the consent of the landlord into occupation. We have stated above that if the tenant continues to be in possession after the expiration of tenancy and pays the rent to the landlord, the tenancy may be one from year to year or from month to month. During a period when the tenant is in possession after expiry of the period, if the tenant stays with the consent of the landlord till such time as further period is fixed or a fresh contract is made, the tenant is called a tenant-at-will. The landlord will decide for what further period shall the tenancy be given. 'A tenancy-at-will is implied when a person is in possession by the consent of the owner and is not held in view of any tenancy for a certain time. The tenancy-at-will does not mean that the landlord has to give a proper notice to quit. The tenant-at-will cannot sublet during that period because no valid contract for further extension in his favour has been made. The death of the landlord or tenant determines the tenancy, i.e., the tenancy comes to an end.
  - (c) *A tenancy by sufferance:* This is a tenancy which is created by fiction of law. If a tenant continues to be in possession after the determination of the period of the lease without the consent of the landlord, he becomes a tenant by sufferance. A tenant-at-will is in possession with the consent of the landlord, whereas a tenant by sufferance is in possession without his permission after the term of the lease comes to an end. This type of tenant is not regarded as a trespasser because the tenant had in his favour a valid lease to start with. No notice is necessary to such a tenant for eviction. This tenant is not responsible for rent. He is liable to pay compensation for use and occupation of the land.
- (v) *Requirements of a valid notice:* In order that a notice to quit is valid it must be a proper notice. The notice must convey the intention to terminate the tenancy as a whole and must specify the date on which the tenancy would expire. As mentioned earlier, if the lease is a lease from month to month, 15 days, notice is required. If it is from year to year 6 months' notice is required. A lease of the moveable property for agricultural or manufacturing purposes shall be deemed to be a lease from year to year. The notice should expire with the end of the period of the tenancy. If it is a lease from month to month and the notice is given by the landlord, the tenant should be asked to quit at the end of the month of the tenancy. The landlord cannot ask his tenant to quit at any time before the expiry of a month or a year of the tenancy.
- (vi) *Determination of leases:* Section 111 of the Transfer of Property Act spells out the various contingencies in which a lease comes to an end. A lease is determined, i.e., comes to an end in the following ways:
- (1) *By efflux of time or lapse of time:* A lease for a definite period, such as a lease for a year, or for a term of years, expires on the last day of the term and the lessor or any person entitled to get back the property may enter without notice or any other formality. Since a lease is a transfer of interest in the property, if during the period for which a lease is valid, the lessee dies, the heirs of the lessee can continue the lease till the expiry of the period.
  - (2) *By the happening of a special event:* When a lease is granted subject to the happening of an event, it comes to an end when the event takes place. Thus, if B grants lease to A for life, it comes to an end on the death of A. Similarly, if a lease is granted for the duration of the war, it comes to an end when the war ends. Where the interest of the lessor is limited, the lease comes to an end when he

loses the interest or where he does not have any power to grant a lease. For example, a tenant for life can grant a lease only to last during his life time. It comes to an end on his death.

- (3) *Merger:* A lease comes to an end when the lessee buys the property of the lessor or when the lessee takes the lessor's interest by succession. Here the right of the lessee merges in that of the lessor. Naturally, the lessee becomes the owner of the property after he acquires it. So there will be no more a lease.
- (4) *By surrender:* A lease may come to an end by surrender. Surrender may be either express or implied. Express surrender arises when the lessee yields up his interest under a lease by mutual consent. Implied surrender occurs, as follows :- if during the subsistence of the lease, a new lease is granted to the tenant to commence at once in substitution for the existing lease, it operates as a surrender of the old lease. For example, a lessee, accepts to take effect during the continuance of the existing lease. This is an implied surrender of the former lease and such lease comes to an end. Similarly, when the landlord reserves possession without any objection on the tenant's part, there is a surrender by implication. Mere non-payment of rent does not amount to surrender.
- (5) *By forfeiture:* A lease also comes to an end by forfeiture. A forfeiture occurs when there is breach of a condition in a lease contract by the lessee. Under the Transfer of Property Act, forfeiture occurs in the following circumstances—the first case in which forfeiture occurs is the case when the lessee breaks an express condition which may be of various types such as, if the lessee does not pay the rent regularly, or if the lessee becomes insolvent, or where the lessee sublets the property to another person. In all such cases there will be a forfeiture. But the condition that the lessee breaks must be an express condition which must have been incorporated in the contract of lease. Then only the lessor can re-enter the leased property and claim that the lease shall be forfeited.

In the case of a forfeiture due to default in payment of the rent, if the lessor sues the lessee to quit, the Court can direct the lessee to pay the rent or arrears of rent and continue the lease. But in a breach of any other condition, such as the breach of a condition preventing the lessee from subletting the property, the Court will not help the lessee if he breaks the condition. He will incur forfeiture. A breach of condition by the lessee gives an option to the lessor to bring the lease to an end. But if he does not exercise the option the lease will continue validly. The lessee, however, cannot on breaking the condition, take advantage of his wrong and terminate the lease.

The second case of forfeiture occurs when the tenant denies the title of the landlord and claims that somebody else or he himself is the owner of the property. In order that a denial of the landlord's title should work as a forfeiture of the lease, three things are necessary:

- (a) the tenant must set up title either in himself or in a third-party;
- (b) the denial must be direct and not casual;
- (c) it must be made known to the landlord.

(vii) *Duties of the Lessor:* Following are some of the duties of the lessor:

- (a) The lessor is bound to disclose to the lessee any material defect in the property with reference to its intended use of which the lessor is and the lessee is not aware. This rule applies only to physical defects of the property such as the condition and the nature of the property leased. You will note that the lessor is not bound to disclose whether or not he has title to the property.
- (b) The next duty of the lessor is to put the lessee in possession of the property. A lease is a transfer of possession the consideration being rent and, therefore, it follows that the landlord cannot recover the rent unless he has delivered possession to the tenant. If a contract of lease has been executed and the lessor does not give possession of the property to the lessee, the lessee can sue the lessor for possession.

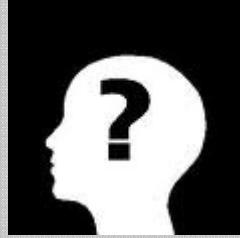
- (c) The next duty that is cast on the lessor is what is usually called covenant for quiet enjoyment. The covenant, that is the right to undisturbed possession, so long as the lessee pays the rent, presupposes possession and, therefore, no action can be brought on this covenant unless the lessee has first obtained possession. The covenant for possession gives the lessee the right to obtain possession; the covenant for quiet enjoyment gives the lessee a right to continue in such possession. If the lessee's possession is disturbed, he can sue for damages or, in case a part of the leased property is taken possession of either by the lessor or by any third-party; the lessee can hold a part of the leased property and pay a proportionate rent.
- (viii) *Duties of the lessee:* The lessee has the following duties:
- The lessee is bound to disclose to the lessor any fact as to nature or extent of the interest that the lessee is about to take, of which the lessee is, and the lessor is not aware and which materially increases the value of such interest.
  - The lessee is bound to pay or tender at the proper time and place, the premium or rent to the lessor or his agent in this behalf. We have already seen that in case the lessee does not pay the rent, he may incur forfeiture of the tenancy. The liability to pay the rent commences from the date the tenant is put into possession.
  - The next duty of the lessee is that he uses the property as a person of ordinary prudence would make use of. But he shall not permit another person to use the property for purposes other than that for which it was leased.
  - He should not do any act which is destructive of or permanently injurious to the property.
  - The lessee must not, without the lessor's consent, erect on the property any permanent structure except for agricultural purpose. If he wants to erect certain fixtures or chattel on the leased property, it must be done without causing any damage to the property. Before the termination of the lease, he can remove all the things attached to the earth. If permanent fixtures are to be made, the lessee must obtain the consent of the landlord.
  - If the lessee comes to know of any proceedings by way of suit to recover the property of the lessor, the lessee should immediately inform the lessor. Since, the tenant is in possession of the property he is the person who is not likely to know of any encroachment on the landlord's property and he should therefore inform the landlord.
  - The lessee should hand over the property at the end of the lease.
- (ix) *Rights of the lessee:* The lessee enjoys the following rights:
- If during the continuance of the lease any accession is made to the property, such accession is deemed to be comprised in the lease, the lessee has a right to enjoy the accretions of the leased property.
  - Where, under the contract, the landlord has agreed to repair the property, the lessee can carry out the repairs and deduct the expenses from the rent if the landlord fails to do so.
  - If the lessee has made payment which the lessor is bound by law to pay such as payment of Government revenues or municipal taxes on the property, the lessee can deduct the amount from the rent and pay the balance to the lessor. He can even take interest on the amount he has paid.
  - The lessee has a right to remove the fixtures he has erected during the term of the lease.

- (e) If, due to no fault of his, the lease comes to an end (i.e., when the lease is of uncertain duration), the lessee or his legal representatives are entitled to all the crops planted or grown by the lessee. The lessee or his representatives have got a right to come and carry away the crops, etc., which are growing on the land. If the lease is of a definite period, such a right cannot be claimed, particularly, when lessee has committed a fault, e.g., where he has committed a breach of a condition entailing forfeiture.
- (f) The lessee may avoid the lease, if property is wholly or partly destroyed by tempest, flood, or fire so as to make it impossible to continue the lease for the purpose for which it was let.
- (g) The lessee has right to transfer absolutely or by way of mortgage or sub-lease, the whole or any part of his interest in the property. We have also noticed that the lessee's rights are transferable.

### ***Test your knowledge***

#### ***Choose the correct answer***

*Which section of the Transfer of Property Act deals with the various contingencies in which a lease comes to an end?*



- (a) Section 121
- (b) Section 112
- (c) Section 111
- (d) Section 222

***Correct Answer: c***

### ***5. Actionable Claims***

"Actionable claim" has been dealt with under Sections 130 to 137 of the Act.

- (i) *Definition:* "Actionable claim" is defined in Section 3 of the Transfer of Property Act as follows:

A claim to any debt, other than a debt secured by mortgage of immoveable property or by hypothecation or pledge of moveable property, or to any beneficial interest in moveable property not in the possession, either actual or constructive, of the claimant, which the Civil courts recognize as affording grounds for relief, whether such debt or beneficial interest be existent, accruing, conditional or contingent.

Actionable claims are claims, to unsecured debts. If a debt is secured by the mortgage of immoveable property it is not an actionable claim, because the Section clearly excludes such a debt. A debt is a liquidated money obligation which is usually recoverable by a suit. To create a debt, first of all, there must be a liquidated or definite sum which is actually due. For example, arrears of rent due. The term debt may also include a sum of money which is due in the sense that it exists, but is not actually payable until a later date. For example, A borrows money from B on the 1st of January and promises to repay on March 15, the amount is not payable till the 15th of March, but certainly it is a debt and it is an accruing debt. Another essential of an actionable claim is that it is not in possession of a person and the person can claim such a debt by bringing an action in a Court of law.

The Section also says that it must be a claim to any debt which the Civil Courts recognise as affording grounds for relief to the person who claims it.

Illustrations of actionable claims:

- (i) Arrears of rent accrual constitute a 'debt' so it is an actionable claim (*Sheu Gobind Singh v. Gauri Prasad*, AIR 1925 Pat. 310).
- (ii) Provident Fund that is standing to the credit of a member of the Provident Fund.
- (iii) Money due under the Insurance Policy.
- (iv) A partner's right to sue for accounts of dissolved partnership is an actionable claim being a beneficial interest in moveable property not in possession (*Thakardas v. Vishindas*).

#### **Non-actionable claims**

- (i) Debentures are secured debts and therefore not regarded as actionable claims.
- (ii) **Copy right though a beneficial interest in immoveable property is not an actionable claim since the owner has actual or constructive possession of the same (*Savitri Devi v. Dwarka Bhatya*, (1939) All 305).**

Again, an actionable claim includes a beneficial interest in the moveable property not in possession. Now, a benefit of a contract for the purchase of goods is a beneficial interest in moveable property.

#### **6. Mortgages**

Sections 58 to 104 of the Act deal with "Mortgages".

##### *Definition and nature of mortgage:*

According to Section 58 of the Transfer of Property Act, a "mortgage" is the transfer of an interest in specific immoveable property for the purpose of securing the payment of money advanced or to be advanced by way of loan, an existing or future debt or the performance of an engagement which may give rise to pecuniary liability.

The transferor is called a mortgagor, the transferee a mortgagee. The principal money and interest the payment of which is secured for the time being are called the mortgage money and the instrument by which the transfer is effected is called a mortgage deed.

##### *Essentials of a mortgage:*

- (1) *Transfer of interest:* The first thing to note is that a mortgage is a transfer of interest in the specific immoveable property. The mortgagor as an owner of the property is possessed of all the interests in it, and when he mortgages the property to secure a loan, he only parts with an interest in that property in favour of the mortgagee. After mortgage, the interest of the mortgagor is reduced by the interest which has been transferred to the mortgagee. His ownership has become less for the time being by the interest which he has parted with in favour of the mortgagee. If the mortgagor transfers this property, the transferee gets it subject to the right of the mortgagor to recover from it what is due to him, i.e., the principal plus interest.
- (2) *Specific immoveable property:* The second point is that the property must be specifically mentioned in the mortgage deed. Where, for instance, the mortgagor stated "all of my property" in the mortgage deed, it was held by the Court that this was not a mortgage. The reason why the immoveable property must be distinctly and specifically mentioned in the mortgage deed is that, in case the mortgagor fails to repay the loan the Court is in a position to grant a decree for the sale of any particular property in a suit by the mortgagee.

(3) *To secure the payment of a loan:* Another characteristic of a mortgage is that the transaction is for the purpose of securing the payment of a loan for the performance of an obligation which may give rise to pecuniary liability. It may be for the purpose of obtaining a loan, or if a loan has already been granted to secure the repayment of such loan. There is thus a debt and the relationship between the mortgagor and the mortgagee is that of debtor and creditor. When A borrows 100 bags of paddy and further quantity by way of interest, it is mortgage transaction for the performance of an obligation.

Where, however, a person borrows money and agrees with the creditor that till the debt is repaid he will not alienate his property, the transaction does not amount to a mortgage. Here the person merely says that he will not transfer his property till he has repaid the debt; he does not transfer any interest in the property to the creditor. In sale as distinguished from a mortgage, all the interest or rights of ownership are transferred to the purchaser. In a mortgage, as stated earlier, only part of the interests are transferred to the mortgagee, some of them remaining vested in the mortgagor.



To sum up, it may be stated that there are three outstanding characteristics of a mortgage:

- (a) the mortgagee's interest in the property mortgaged terminates upon the performance of the obligation secured by the Mortgage.
- (b) the mortgagor has a right of foreclosure upon the mortgagor's failure to perform.
- (c) the mortgagor has a right to redeem or regain the property on repayment of the debt or performance of the obligation.

#### *Form of a mortgage contract:*

According to Section 59, where the principal money secured is Rs. 100 or upwards, a mortgage, other than a mortgage by deposit of title-deeds, can be effected only by a registered instrument or by delivery of property. It should be noted that a mortgage is not a mere contract but it is the *Conveyance of Interest* in the mortgaged property and as soon as the mortgage deed is registered an interest in the property vests in the mortgagee.

#### *Kinds of mortgages:*

There are in all six kinds of mortgages in immoveable property, namely

- (a) Simple mortgage.
- (b) Mortgage by conditional sale.
- (c) Usufructuary mortgage.
- (d) English mortgage.
- (e) Mortgage by deposit of title-deeds or equitable mortgage.
- (f) Anomalous mortgage.

#### *(a) Simple mortgage*

In a simple mortgage, the mortgagor binds himself personally to pay the debt and agrees in the event of his failure to pay the mortgage money, the mortgagee shall have the right to cause the property to be applied so far as may be necessary by means of a decree for the sale of property. If the mortgaged property is not sufficient to discharge the debt, the mortgagee can bring a personal action against the mortgagor and obtain a decree which, like any other money decree, can be executed against other properties of the mortgagor. In simple mortgage, no right of possession or foreclosure is available to the mortgagee.

**(b) Mortgage by conditional sale**

In this type of mortgage, the property is mortgaged with a condition super added that in the event of a failure by the debtor to repay the debt at the stipulated time, the transaction should be regarded a sale, and in case the loan is repaid at the stipulated time, the sale shall be invalid, or on condition that on such payment being made the buyer shall transfer the property to the seller.

Thus, for all practical purposes, this type of mortgage is ostensible sale of the mortgaged property with a condition for re-purchase by the mortgagor by repaying the loan. It will be noted that the mortgagor transfers the property with the following three conditions:

- (a) If the loan is repaid, the sale becomes void.
- (b) If the loan is not repaid at the stipulated time, the sale will become absolute and binding.
- (c) When the debt has been repaid at the stipulated time, the mortgagee shall re-transfer the property to the mortgagor.

In case of mortgage by conditional sale, there is no personal covenant. That is unlike in the case of a simple mortgage, the mortgagor in this case does not bind himself personally to repay the debt. The mortgagee is not given the possession of the property in this type of mortgage. This is also the position in the case of a simple mortgage. Again, in a mortgage by conditional sale, the mortgagee's remedy is 'foreclosure', that is he becomes the owner of the property in default of payment of the debt by the mortgagor, he has to institute a regular suit in a Court of law to "foreclose" the mortgage. To "foreclose" means to debar the mortgagor from redeeming the property forever.

**(c) Usufructuary mortgage**

Section 58(d) defines a "usufructuary mortgage" as "where the mortgagor delivers possession or expressly or by implication binds himself to deliver possession of the mortgaged property to the mortgagee, and authorises him to retain such possession until payment of the mortgage money, and to receive the rents and profits accruing from the property or any part of such rents and profits and to appropriate the same in lieu of interest, or in payment of the mortgage money, or partly in lieu of interest or partly in payment of the mortgage money, the transaction is called an usufructuary mortgage. It is also called a mortgage with possession.

Thus in this type of mortgage the mortgagor has to deliver possession of the property to the mortgagee. If the possession is not given, the mortgagee can sue for possession. The mere fact that possession has not been delivered will not alter the nature of the transaction. **In *Pratap Bahadur v. Gajadhar*, 24 All 521, it was agreed that the mortgagee will put the mortgagor in possession of a village on a certain date and to pay interest till possession was delivered. It was held that mortgage was an usufructuary mortgage.** The mortgagee is authorised to retain possession and receive rents, etc., until he recovers the whole debt and the interest. The usufructuary mortgagee has to look only to the profits that arise out of the property for realising his debt; there is no personal liability on the part of the mortgagor. Similarly, the mortgagee has no right to foreclose the mortgage or to sue for sale.

A mortgage may be regarded as usufructuary even though the entire debt is not to be paid out of the profits of the property. Therefore, a usufructuary mortgage may be either (i) where the entire mortgage money is to be paid from the profit of the land; or (ii) where only part of the mortgage money is principal or interest amount is to be paid from the profit of the land.

If in a usufructuary mortgage a time is mentioned during which the mortgagee should recover the debt, etc., then after the time is over, the mortgagee should deliver back the property to the mortgagor. He cannot refuse to give back the property, if he has not been able to recover the debt and the interest, etc. A usufructuary mortgagee is supposed to remain in possession of the mortgaged property and manage the same as a person of ordinary prudence would manage subject to the conditions of mortgage agreement. Any loss due to failure on his part would be debited to his account (*Panchanan Sharma v. B.P. Jagnani*, SCALE 1995 (2) 641).

Thus, a usufructuary mortgage has the following characteristics:

1. Possession of property must be delivered to the mortgagee;
2. There is no personal liability on the part of the mortgagor to pay;
3. The mortgagee is entitled to rents and profits in lieu of interest or principal or both; and
4. The mortgagee however is not entitled to foreclose the mortgagee or to sue for sale.

**(d) English mortgage**

Section 58(e) states that: "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 retransfer it to the mortgagor upon payment of the money as agreed, the transaction is called an English mortgage".

Here the mortgagor transfers the ownership of the property as security and the mortgagee promises to re-transfer the ownership, if the money is paid within a definite time. There is also a personal covenant as the mortgagor promises to repay within a certain date. In this type of mortgage, there is proviso that if money is repaid the property would be reconveyed. The remedy of the mortgagee is sale of the property to recover the debt. Thus, the essential features of an English mortgage are as under:

1. The mortgagor binds himself to repay the mortgage money on a certain day. In other words, there should be a personal undertaking to pay.
2. The mortgaged property is absolutely transferred to the mortgagee.
3. Such absolute transfer is subject to a proviso that the mortgagee will reconvey the property to the mortgagor upon payment by him of the mortgage money on the fixed day.

***Distinction between English mortgage and mortgage by conditional sale***

An English mortgage looks like a mortgage by conditional sale but there are obvious differences between the two:

1. In English mortgage there is a personal liability undertaken by the mortgagor to pay the debt. In a mortgage by conditional sale there is no personal covenant (agreement for payment of the mortgage money and mortgagee has his remedy against the mortgaged property only);
2. In English mortgage the ownership in the mortgaged property is absolutely transferred to the creditor (i.e. mortgagee) which however, may be divested on repayment of the loan on the fixed day.

In a mortgage by conditional sale, the mortgagee gets only a qualified ownership which may, however, ripen into an absolute ownership in default of payment of the mortgage money.

***Test your knowledge***

***Choose the correct answer***

*In which of the following mortgages, the ownership in the mortgaged property is absolutely transferred to the creditor?*

- (a) Simple mortgage
- (b) English mortgage
- (c) Anomalous mortgage
- (d) Usufructuary mortgage

***Correct Answer: (b)***



**(e) Mortgage by deposit of title deeds**

This type of mortgage is called *equitable mortgage* in English law. In this transaction, a person delivers to the creditor or his agent documents of title of his immoveable property with an intention to create a security, and obtains a loan. The requisites of such a mortgage are (i) a debt, (ii) deposit of title deeds, and (iii) an intention that the deeds shall be security for the debt.

In order that a valid mortgage on an immoveable property should be effected, it must be in writing and attested by two witnesses and the document must be registered. But in case of a mortgage by deposit of title deeds, it need not be registered and an oral agreement between the person and the creditor followed by the delivery of the documents of title to the property is enough. The creditor will have the possession of the documents and he will advance the money at the stipulated rate of interest. In case the mortgagor does not repay the loan, the creditor on the basis of having the title deeds in his possession can sue the debtor to recover the money. This type of mortgage has been recognized due to expediency. Many persons, specially the business people, may need money urgently and they cannot wait till a formal document is written, signed, attested and then registered. So they will simply approach the creditor and hand over the title deeds of their property and borrow money. This avoids delay and other formalities for effecting a valid mortgage.

There must be a clear intention on the part of the person who hands over the title deeds to effect a valid mortgage. In the absence of any intention, the mere holding in possession of the title deeds will not create a valid mortgage.

The term 'documents of title' or title deeds means such documents as will show *prima facie* or apparent title to the property of the person who is borrowing money. Accordingly, in one case it was held that tax receipt was not a document of title to the property on which the tax was paid. What is necessary to deposit is a document which gives him his right to the property and the creditor should insist on the production of this document before he gives money on a pledge of documents.

It should be noted that this type of mortgage can be created only in certain towns and not everywhere in India. The facility to create a valid mortgage is available in the following towns in India: Calcutta, Madras, Bombay, Adoni, Ajmer, Allahabad, Alwar, Bangalore, Bellary, Cochin, Coimbatore, Delhi, Jaipur, Jodhpur, Kanpur, Rajahmundry, Udaipur, Vellore, Ellora, Pali, Bhilwara, Bikaner, Kakinada, Narayanganj, Mysore, and Madurai. Though this type of mortgage is limited to specific cities it is at par with any other legal mortgage (*K.J. Nathan v. S.V. Maruthi Rao*, A.I.R. 1965 S.C. 443).

Title deeds should be delivered in these areas, the property of the person may be situated elsewhere. If the deposit of title deeds has taken place in *any other town*, it will not be a valid mortgage. Similarly, if the property is situated in any one of the towns mentioned above, but the deposit of title deeds is made in other towns or areas then again it will not be a valid mortgage.

**(f) Anomalous mortgage**

Section 58(g) of the Transfer of Property Act provides that "a mortgage which is not a simple mortgage, a mortgage by conditional sale, usufructuary mortgage, an English mortgage, or a mortgage by deposit of title deeds within the meaning of this section is called an anomalous mortgage".

Thus, an anomalous mortgage is a combination of various other mortgages, for example, a usufructuary mortgage may be created and the mortgagee shall have the right of sale. You have already noticed that in a usufructuary mortgage only possession is given to the mortgagee and there is no right of sale. But in an anomalous mortgage the right of sale along with the possession of the property may be given. You have also seen that in the case of usufructuary mortgage, there is no personal liability on the part of a mortgagor but if the mortgagor assumes personal liability to pay the mortgage money, it will be an anomalous mortgage.

Again, a mortgagee may be given possession of the property for a fixed period with a condition that in case the debt is not discharged at the expiry of the period mentioned, the mortgage shall be regarded as a mortgage by conditional sale. In this case, the mortgage has got a right of "foreclosure" and after the expiry of the period if the debt is not paid, the mortgagee will become the owner of the property.

Two other terms in common use in connection with mortgage may be considered here. These terms are (i) Sub-mortgage; and (ii) Puisne mortgage.

*Sub-mortgage:*

Where the mortgagee transfers by mortgage his interest in the mortgaged property, or creates a mortgage of a mortgage the transaction is known as a sub-mortgage. For example, where A mortgages his house to B for Rs. 10,000 and B mortgage his mortgagee right to C for Rs. 8,000. B creates a sub-mortgage.

*Puisne mortgage:*

Where the mortgagor, having mortgaged his property, mortgages it to another person to secure another loan, the second mortgage is called a puisne mortgage. For example, where A mortgages his house worth Rs. one lakh to B for Rs. 40,000 and mortgages the same house to C for a further sum of Rs. 30,000, the mortgage to B is first mortgage and that to C the second or puisne mortgage. C is the puisne mortgagee, and can recover the debt subject to the right of B, the first mortgagee, to recover his debt of Rs.40,000 plus interest.

***Test your knowledge***

***Choose the correct answer***

*Which of the following mortgages is called equitable mortgage in English law?*

- (a) Simple mortgage
- (b) English mortgage
- (c) Anomalous mortgage
- (d) Mortgage by deposit of title deeds



***Correct Answer: (d)***

***Rights of mortgagor:***

By mortgaging the property the mortgagor does not cease to be its owner, he only transfers an interest in it. The law, therefore, grants him the following rights:

- (a) *Right of redemption:* The first and the most important right of the mortgagor is the right to redeem i.e., take back the mortgaged property by paying the mortgage money at any time after the stipulated date for repayment. Section 60 of the Act provides that any time after the principal amount has become due, the mortgagor has a right to redeem the property. Although the Act gives him the right to redeem "any time" after their debt has become due, it enjoins upon the mortgagor the obligation to exercise this right (i) before the right is extinguished by the Act of parties or by a decree of Court, or (ii) before it is barred by the Limitation Act. According to the Law of Limitation the, mortgagor can redeem the property within 60 years after the money has become due. This right to redeem the property even after the time of payment has elapsed is called the Right or Equity or Redemption. But the *mortgagor is not entitled to redeem before the mortgage money becomes due*

*on the date fixed for repayment of the loan.* His right to redeem arises only when mortgage money becomes due and not before.

- (b) *Right against clog on equity of redemption:* Right of redemption or equity of redemption is the essence of a mortgage, and any provision inserted in the mortgage deed to prevent, evade or hamper redemption is void. Any condition which prevents the mortgagor from redeeming the property is called a "clog" on the equity or right of redemption and is void. The rule of equity that *once a mortgage always a mortgage* prohibits a clog on the right of redemption. In other words, once a transaction is found to be a mortgage, the Court would not permit any condition in a mortgage deed which would prevent or impede redemption or repayment of the loan for which the security was given.
- (c) *Right of partial redemption:* A mortgage, as a rule, being one and indivisible for the debt and every part of it, the mortgagor cannot redeem piecemeal; he must redeem the whole property. But Section 61 of the Act gives a right of partial redemption stating that "a mortgagor who has executed two or more mortgages in favour of the same mortgagee shall, in the absence of a contract to the contrary, when the principal money of any two or more of the mortgages has become due, be entitled to redeem any one such mortgage separately or any two or more of such mortgages together."

*Implied contract by mortgagor:*

The parties are free to enter into any terms they like. Where, however, the contract does not contain all the terms, Section 65 provides for implied terms as follows:

In the absence of a contract to the contrary, the mortgagor shall be deemed to have contracted with the mortgagee that the :

- (a) mortgagor is entitled to transfer the interest (covenant for title);
- (b) mortgagor will assist the mortgagee to enjoy quiet possession;
- (c) mortgagor will pay public charges in respect of the mortgaged property;
- (d) mortgagor covenants as to payment of the rent due on lease where, the mortgaged property is leased;
- (e) mortgagor covenants as to payments of interest and principal on prior encumbrances, where the mortgage is a second or subsequent encumbrance on the property.

*Rights of mortgagee and his remedies:*

If the mortgagor does not pay the mortgage money, the mortgagee may proceed to recover (i) from the mortgaged property, or (ii) sue for recovery from the mortgagor personally. Thus the mortgagor has two remedies: one against the property and the other against the mortgagor personally.

## 7. Charges

*Meaning of charge:* "Charge" has been defined under Section 100 as follows: "Where immoveable property of one person is by the act of parties or operation of law made security for the payment of money to another, and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property".

As is evident from the above definition, a charge comes into existence either by the act of parties or by operation of law.

*Charge by act of parties:* When in a transaction for value, both the parties (debtor and creditor) intend that the property existing or future shall be made available as security for the payment of a debt and that the creditor shall have a *present right* to have it made available, there is a charge.

*Charge by Operation of Law:* Charges created by law are those which arise on account of some statutory provisions. They are not created by the voluntary action of parties but arise as a result of some legal obligation.

*Floating charge:* A charge may be floating as well as fixed. A fixed charge is a charge on specific property but a floating charge is an equitable charge on the assets for time being of a going concern. It is peculiar to companies which are able to borrow money without any interference with their assets so long as they are going concern. In other words, it is a charge on a class of the assets of the company, present as well as future. The assets of the company are constantly undergoing a change but the creditors will not normally interfere with the assets of the company unless there is breach of some condition. As Professor Gower says, the assets are liquid and the charge is floating. It is ambulatory and shifting in its nature hovering over and so to speak floating with the property which it is intended to effect. As it does not attach to any specific property, it remains document until it crystallises.

A floating charge has the following characteristics:

1. It is a charge on class of assets both present and future.
2. The class of assets charged is one which in the ordinary course of business would be changing from time to time.
3. It is contemplated by the charge that until some future step is taken by those who are interested in the charge the company may carry on its business in the ordinary way, i.e., it may use its assets charged in the ordinary course of its business. (Per Roman L.J. in *Reyork Shive Wool Combers Associated Limited*, (1903) 2 Ch. 284) **A floating charge is created by debentures on the company's undertaking or its estate, property and effects. It is not necessary that the charge should be on all company's assets. Thus a mortgage of a cinema and of the chattels used in the cinema premises was held to be a floating charge as to the chattels (*National Provisional Bank of England Limited v. Charteb Electric Theatres Limited*, (1916) Ch. 132).** Similarly, a floating charge was created by a mortgage of book and other debts which shall become due during the continuance of this security (*Reyork Shive Wool Combers Association, Supra*).

#### *Crystallisation of floating charge*

A floating charge becomes fixed or crystallises in the following cases:

1. When the money becomes payable under a condition in the debenture and the debenture holder, (i.e., the creditor) takes some steps to enforce the security;
2. When the company ceases to carry on business; and
3. When the company is being wound-up.

#### ***Test your knowledge***

***State whether the following statement is “True” or “False”***

*A floating charge becomes fixed or crystallises when the company ceases to carry on business.*

- *True*
- *False*

***Correct Answer: True***



### 8. Distinction between Mortgage and Charge

Although in a charge, the property is made a security for the payment of the loan, yet the transaction does not amount to mortgage. It is important, therefore to distinguish between a charge and mortgage.

- (a) A mortgage is transfer of an interest in the property made by the mortgagor as a security for the loan, while the charge is not the transfer of any interest in the property though it is security for the payment of an amount.
- (b) A charge may be created by act of parties or by operation of law. A mortgage can only be created by act of parties.
- (c) A mortgage deed must be registered and attested by two witnesses, while a charge need not be made in writing, and if reduced to writing, it need not be attested or registered.
- (d) In certain types of mortgage (viz., mortgage by conditional sale and anomalous mortgage) the mortgagor can foreclose the mortgaged property but in charge, the charge-holder cannot foreclose though he can get the property sold as in a simple mortgage.
- (e) From the very nature of it, a charge as a general rule, cannot be enforced against a transferee for consideration without notice. But in a mortgage, the transferee of mortgaged property from the mortgagor, can only acquire the remaining interest of the mortgagor, and is therefore, only bound by the mortgage.
- (f) In a charge created by act of parties the specification of the particular fund or property negatives a personal liability and the remedy of the charge-holder is against the property only. In a mortgage, there can be security as well as personal liability. In fact, the absence of a personal liability is the principal test that distinguishes a charge from a simple mortgage.

### LESSON ROUND-UP

- The law relating to transfer of property is governed by the Transfer of Property Act, 1882. 'Transfer of Property' means an act by which a living person conveys property, in present or future, to one or more other living persons, or to himself, and one or more other living persons. 'living person' includes a company or association or body of individuals, whether incorporated or not.
- Every person who is competent to contract and entitled to transferable property, or authorized to dispose of property is competent to transfer such property. Property can be transferred either orally or by writing. Moveable property can be transferred by delivery of possession or by registration. In the case of *tangible* immoveable property of the value of one hundred rupees and upwards, or in the case of a *reversion* or other *intangible* thing, transfer can be made only by a registered instrument. In the case of *tangible* immoveable property of a value less than one hundred rupees, such transfer may be made either by a registered instrument or by delivery of the property.
- When property is transferred, the transferee should not be restrained absolutely from alienating the property. One may give property to another subject to a condition, but the condition should not be one which absolutely prevents the transferee from alienating the property. A transfer may also be made subject to a contingency which may or may not occur. This is known as condition subsequent. Condition subsequent is one which destroys or divests the rights upon the happening or non-happening of an event.
- Section 35 of the Transfer of Property Act deals with what is called doctrine of election. Election may be defined as "the choosing between two rights where there is a clear intention that both were not intended to be enjoyed". The foundation of doctrine of election is that a person taking the benefit of an instrument must also bear the burden, and he must not take under and against the same instrument.

- Where, with the consent, express or implied, of the persons interested in immoveable property, a person is the ostensible owner of such property and transfers the same for consideration, the transfer shall not be voidable on the ground that the transferor was not authorized to make it, provided that the transferee, after taking reasonable care to ascertain that the transferor had power to make the transfer, has acted in good faith. This is called doctrine of Holding Out.
- Doctrine of Feeding the Grant by Estoppel means where, a person fraudulently or erroneously represents that he is authorized to transfer certain immoveable property and professes to transfer such property for consideration, such transfer shall, at the option of the transferee, operate on any interest which the transferor may acquire in such property at any time during which the contract of transfer subsists.
- Where a person transfers his property so that his creditors shall not have anything out of the property, the transfer is called a fraudulent transfer. A debtor in order to defeat or delay the rights of a creditor, may transfer his property to some person, who may be his relative or a friend. The law does not allow this.
- The Act does not allow accumulation of income from the land for an unlimited period without the income-being enjoyed by owner of the property. The law allows accumulation of income for a certain period only. The period for which such accumulation is valid is : (a) the life of the transferor, or (b) eighteen years from the date of transfer. Any direction to accumulate the income beyond the period mentioned above is void. However, this is subject to certain exceptions.
- *Lis pendens* means a pending suit, action, petition or the like. Section 52 of the T.P. Act incorporates the doctrine of *Lis pendens*. It states that during the pendency of a suit in a court of law, property which is subject to a litigation cannot be transferred.
- The Act expressly provides for special types of transfers such as sale, exchange, gift, mortgage and lease. In a sale, exchange and gift, there is a transfer of the ownership of property but mortgage is a transfer of an interest in specific immovable property and lease is a transfer of the right to enjoy immoveable property.
- Actionable claims are claims, to unsecured debts. If a debt is secured by the mortgage of immoveable property it is not an actionable claim, because the Section clearly excludes such a debt.
- Charge under the Act has been defined as “where immoveable property of one person is by the act of parties or operation of law made security for the payment of money to another, and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property”.
- As is evident from the above definition, a charge comes into existence either by the act of parties or by operation of law. A charge may be floating as well as fixed. A fixed charge is a charge on specific property but a floating charge is an equitable charge on the assets for time being of a going concern. It is peculiar to companies which are able to borrow money without any interference with their assets so long as they are going concerns.

### SELF-TEST QUESTIONS

1. Discuss the object of the Transfer of Property Act. Distinguish between immoveable and moveable property.
2. What is the subject matter of transfer under the T.P. Act? Discuss properties which cannot be transferred.
3. Define a mortgage. Discuss various types of mortgages.
4. What is the rule against perpetuity?

## 5. Write short notes on

- (i) Puisne mortgage;
  - (ii) Charges under the T.P. Act;
  - (iii) Vested and contingent interest;
  - (iv) Actionable claims.



# Lesson 7

## LAW RELATING TO STAMPS

### LESSON OUTLINE

- Important Definitions
- Instruments chargeable with Duty
- Extent of liability of Instruments to Duty
- Valuation for Duty under the Act
- Apportionment
- Persons liable to pay Duty
- Methods of Stamping
- Use of Adhesive Stamps
- Mode of cancellation of Adhesive Stamps
- Denoting Duty
- Time of Stamping Instruments
- Adjudication as to Stamps
- Instruments not duly Stamped – Treatment and Consequences
- Admission of Instruments
- Admission of Improperly Stamped Instruments
- Dealing with Instruments Impounded
- Prosecution for offences against Stamp Law
- Allowance and Refund
- Criminal Offences, etc.

### **LEARNING OBJECTIVES**

The Indian Stamp Act, 1899 is a fiscal legislation dealing with tax on transactions. The tax is levied on in the shape of stamps recording the transactions. Supreme Court, in the case of *AV Fernandez v. State of Kerala AIR 1957 SC 657*, explained the law relating to interpretation of fiscal statutes as: "In construing fiscal statutes and in determining the liability of a subject to tax one must have regard to the strict letter of the law and not merely to the spirit of the statute or the substance of the law. If the Revenue satisfies the Court that the case falls strictly within the provisions of the law, the subject can be taxed. If, on the other hand, the case is not covered within the four corners of the provisions of the taxing statute, no tax can be imposed by inference or by analogy or by trying to probe into the intentions of the legislature and by considering what was the substance of the matter."

In our country, documents are often executed without proper legal advice and lawyers are faced with a difficult situation when they find that the document to be put in the court is not properly stamped. Sometimes people are unduly taxed by overzealous officers. Therefore, it is essential for the students to be familiar with the law relating to stamp duties.

The Indian Stamp Act, 1899 is the law relating to stamps which consolidates and amends the law relating to stamp duty. It is a fiscal legislation envisaging levy of stamp duty on certain instruments.

## INTRODUCTION

The Indian Stamp Act, 1899 is the law relating to stamps which consolidates and amends the law relating to stamp duty. It is a fiscal legislation envisaging levy of stamp duty on certain instruments. The Act is divided into eight Chapters and there is a schedule which contains the rates of stamp duties on various instruments.

### (a) Union List

Union List, Entry 91 gives power to the Union Legislature to levy stamp duty with regard to certain instruments (mostly of a commercial character). They are bill of exchange, cheques, promissory notes, bill of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies and receipt. The power to reduce or remit duties on these instruments is vested in the Union Government as per Section 9 of the Act.

### (b) The State Legislature

State List, entry 63 confers on the States power to prescribe the rates of stamp duties on other instruments. As per "Principles" for levy of duty fall in the Concurrent List, entry 44.

### (c) Amendments, entry 44

The amendments to the Central Act effected by the States are in the shape of amendment of sections of the Central Act, adding new sections, adding separate schedules, modifying in schedules, etc. Some States, for their convenience, have passed separate legislation to cover the matters coming under State's domain. As a result, the rates of stamp duties in different States on other instruments category differ from State to State for the same instrument.

## IMPORTANT DEFINITIONS

Section 2 of the Act contains definitions of various terms used in the Act. Some important definitions are discussed below:

### Banker

"Banker" includes a bank and any person acting as a banker [Section 3 of the Negotiable Instruments Act defines a banker as including persons or a corporation or company acting as bankers]. [Section 2(1)]

### Bill of Lading

"Bill of Lading" includes a 'through bill lading' but does not include a mate's receipt. [Section 2(4)]

A bill of lading is a receipt by the master of a ship for goods delivered to him for delivery to *X* or his assigns. Three copies are made, each signed by the master. One is kept by the consignor of the goods, one by the master of the ship and one is forwarded to *X*, the consignee, who, on receipt of it, acquires property in the goods. It is a written evidence of a contract for the carriage and delivery of goods by sea, for certain freight.

When goods are delivered on board a ship, the receipt is given by the person incharge at that time. This receipt is known as the mate's receipt. The shipper of the goods returns this receipt to the master before the ship leaves and receives from him bill of lading for the goods, signed by the master.

## Conveyance

The term “conveyance” includes a conveyance on sale and every instrument by which property (whether movable or immovable) is transferred *inter vivos*<sup>1</sup> and which is not otherwise specifically provided for by Schedule. It does not include a will. [Section 2(10)]

Thus, all transfers of property whether movable or immovable, on sale (which are not otherwise specially provided for by the Schedule), are chargeable as conveyances. Transfers which are otherwise provided for in the Schedule are Composition Deed, Exchange of Property, Gift, Lease, Mortgage, Reconveyance, Release, Settlement, Transfer, Transfer of Lease and (Declaration of) Trust.

## Instrument

Section 2(14) defines an “instrument” to include every document by which any right or liability is, or purports to be, created, transferred, limited, extended, extinguished or recorded. The definition is an inclusive definition, and is not necessarily restricted to those documents which are specifically mentioned in the definition. Briefly stated, an instrument includes conveyances, leases, mortgages, promissory notes and wills, but not ordinary letters or memoranda or accounts.

Following instances may be noted:

- (i) An unsigned draft document is not an “instrument” (because it does not create or purport to create any right, etc.).
  - (ii) An entry in a register, containing the terms of hiring of machinery is an “instrument”, where it is authenticated by the thumb impression of the hirer. (Reason is, that it purports to create, a liability etc.)
  - (iii) A letter which acknowledges receipt of a certain sum as having been borrowed at a particular rate of interest and for a *particular period and that it will be repaid with interest on the due date* is an “instrument”.
- [These examples show, that the law looks to the substance and effect (or intended effect) of the text of the instrument and not the physical *medium* through which it is recorded.]
- (iv) Photocopy of an agreement is not an instrument as defined under Section 2(14) of the Act. *Ashok Kalam Capital Builders v. State & Anr.*, AIR 2010 (NOC) 736 (Del).

## Executed / Execution

Under Section 1(12), the words “executed” and “execution” (used with reference to instruments), mean “signed” and “signature” respectively.

Signature includes mark by an illiterate person. [Section 3(52), General Clauses Act, 1897]

An instrument which is chargeable with stamp duty only on being “executed” is not liable to stamp duty until it is signed.

The Collector can receive the stamp duty without penalty and certify an instrument as duly stamped, as from the date of execution. (Sections 37 and 40)

<sup>1</sup> The expression “*inter vivos*” means during lifetime.

## Impressed Stamp

According to Section 2(13), “impressed stamp” includes:

- (a) labels affixed and impressed by the proper officer; and
- (b) stamps embossed or engraved on stamp paper.

**The rules framed under the Act invariably prescribe to what documents impressed stamps are to be used. The term includes both a stamp impressed by the Collector and also a stamp embossed on stamp paper. Special adhesive stamps are labels (*Ganga Devi v. State of Bihar*, 1 LR 45 Pat. 198).**



The instrument is duly stamped if it has been duly stamped at the time of execution and is admissible in evidence, though the stamp is subsequently removed or lost (*Mt. Mewa Kunwari v. Bourey*, AIR 1934 All. 388).

## Bill of Exchange

According to Section 2(2), “bill of exchange” means a bill of exchange as defined in the Negotiable Instruments Act, 1881 and includes also a *Hundi* and any other document entitling or purporting to entitle any person, whether named therein or not, to payment by any other person of, or to draw upon any other person for, any sum of money. The Negotiable Instruments Act, defines a “bill of exchange” as an instrument in writing, containing an unconditional order signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.

### Bill of exchange payable on demand

Under Section 2(3) of the Stamp Act, a “bill of exchange on demand” includes:

- (a) an order for the payment of any sum of money by a bill of exchange or promissory note or for the delivery of any bill of exchange or promissory note in satisfaction of any sum of money, or in the payment of any sum of money out of any particular fund which may or may not be available, or upon any condition or contingency which may or may not be performed or happen;
- (b) an order for the payment of any sum of money weekly, monthly or at any other said period; and
- (c) a letter of credit, that is to say, any instrument by which one person authorises any other person to give credit to the person in whose favour it is drawn.

It may be noted that a bill of exchange payable on demand includes even a letter of credit, as per above definition.

Thus, the definition in the Stamp Act includes many instruments which could not be classed as ‘bills of exchange’ within the definition given by the Negotiable Instruments Act, 1881.

## Cheque

Under Section 2(7) of the Stamp Act, “cheque” means a bill of exchange drawn on specified banker, not expressed to be payable otherwise than on demand. This definition follows the definition given in the Negotiable Instruments Act, 1881.

It should be mentioned that in India, cheques are no longer subject to stamp duty. Entry 21 in the Schedule levying duty on cheque was deleted by Act 5 of 1927.

## Bond

Under Section 2(5), a “bond” includes –

- (a) any instrument whereby a person obliges himself to pay money to another on condition that the obligation shall be void if a specified act is performed, or is not performed, as the case may be;
- (b) any instrument attested by a witness not payable to order or bearer, whereby a person obliges himself to pay money to another; and
- (c) any instrument so attested, whereby a person obliges himself to deliver grain or other agricultural produce to another.

The word “oblige” has been used in all sub-clauses in the definition. Therefore, no document can be a bond unless it is one which, by itself, creates the obligation to pay the money. The words “obliges himself to pay money” make it very clear, that the obligation is not a pre-existing one. Where the liability already exists it cannot be said that under a subsequent document (merely reproducing the nature of the obligation) an obligation has been created.

### Test your knowledge

#### Choose the correct answer

Which of the following is the instrument in writing, containing an unconditional order signed by the maker?

- (a) Bill of Exchange
- (b) Cheque
- (c) Impressed Stamp
- (d) Marketable Security



**Correct answer: (a)**

## Chargeable

Under Section 2(6) “chargeable” as applied to an instrument executed or first executed after the commencement of the Act means chargeable under the Act and as applied to any other instrument, chargeable under the law in force in India when such instrument was executed or where several persons executed the instrument at different times, first executed.

## Lease

“Lease” means a lease of immovable property and includes also:

- (a) a patta;
- (b) a kabuliyat or other undertaking in writing, not being a counterpart of a lease to cultivate, occupy or pay or deliver rent for, immovable property;
- (c) any instrument by which tolls of any description are let;
- (d) any writing on an application for a lease intended to signify that the application is granted. [Section 2(16)]

Section 105 of the Transfer of Property Act defines lease as a transfer of a right to enjoy such property, made for a certain time, expressed or implied, or in perpetuity, in consideration of a price paid or promised, or of money, a share of crops, service or any other thing of value to be rendered periodically or on specified occasions to the transferor by the transferee, who accepts the transfer on such terms.

A *patta* is an instrument given by the Collector of District or any other receiver of the revenue, to the cultivator, specifying the condition or conditions upon which the lands are to be held and the value or proportion of the produce to be paid therefor.

A *Kabuliyat* is executed by the lessee, accepting the terms of the lease and undertaking to abide by them. Although, it is not a lease under Section 105 of the Transfer of Property Act, it is expressly included in the definition for the purposes of the Stamp Act.

*Toll* is a tax paid for some liberty or privilege, such as for passage over a bridge, ferry, along a highway or for the sale of articles in a market or fair or the like. It does not include 'octroi' or 'chungi'.

### Promissory Note

It means a promissory note as defined by the Negotiable Instruments Act, 1881. It also includes a note promising the payment of any sum of money out of a particular fund which may or may not be available, or upon any condition or contingency which may or may not be performed or happen. [Section 2(22)]



*Requisites of a promissory note* as per the Negotiable Instruments Act, 1881 are the following:

- (a) the document must contain an unconditional undertaking to pay;
- (b) the undertaking must be to pay money only;
- (c) the money to be paid must be certain;
- (d) it must be payable to or to the order of a certain person or to bearer;
- (e) the document must be signed by the maker.

### Illustrations

An instrument in the form:

- "I do acknowledge myself to be indebted to B in Rs. 1,000 to be paid on demand for value received" is a promissory note.
- "I have received a sum of £20 which I borrowed from you and I have to be accountable for the sum with interest" held not to be a promissory note.
- "On demand I promise to pay to the trustees of W&C or their treasurer for the time being £100" was held a good promissory note.

### Receipt

"Receipt" includes any note, memorandum or writing:

- (a) whereby any money or any bill of exchange, cheque or promissory note is acknowledged to have been received; or
- (b) whereby any other movable property is acknowledged to have been received in satisfaction of a debt; or

- (c) whereby any debt or demand, or any part of a debt or demand is acknowledged to have been satisfied or discharged; or
- (d) which signifies or imports any such acknowledgement, and whether the same is or is not signed with the name of any person. [Section 2(23)]

A mere acknowledgement in writing of the receipt of *immovable* property will not attract sub-clause (b). Under sub-clause (c), any acknowledgement in satisfaction or discharge of any debt or demand or any part thereof is covered; for instance, a receipt given by the secretary or other manager of a club acknowledging payment of the club dues comes within the sub-clause.

An ordinary cash memo issued by a shopkeeper or another person selling the goods or other merchandise is not a receipt, unless it contains an acknowledgement of receipt of the money.

A letter acknowledging the receipt of money or cheque is a receipt. A document merely saying that the signatory has received a sum of Rs. 500 is a receipt.

### Settlement

“Settlement” means any non-testamentary disposition, in writing, of movable or immovable property made:

- (a) in consideration of marriage;
- (b) for the purpose of distributing property of the settler among his family or those for whom he desires to provide, or for the purpose of providing for some person dependent on him; or
- (c) for any religious or charitable purpose;

and includes an agreement in writing to make such disposition. [Section 2(24)]

The definition of “settlement” excludes a will. A will is intended to operate only on death, while a settlement operates immediately.

### Marketable Security

Under Section 2(16A), “marketable security” means a security of such a description as to be capable of being sold in stock market in India or in the United Kingdom.

### Stamp

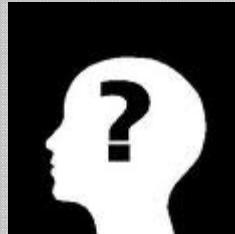
“Stamp” means any mark, seal or endorsement by any agency or person duly authorized by the State Government and includes an adhesive or impressed stamp for the purposes of duty chargeable under this Act. This definition of the stamp has been inserted by the Finance (No. 2) Act, 2004.

#### Test your knowledge

##### Choose the correct answer

Which of the following is a note promising the payment of any sum of money out of a particular fund which may or may not be available?

- (a) Promissory Note
- (b) Chargeable
- (c) Lease
- (d) None of the above



Correct answer: (a)

## INSTRUMENTS CHARGEABLE WITH DUTY

Section 3 of the Act is the charging section. It provides that subject to the provisions of the Act and the exemptions contained in Schedule I, the following instruments shall be chargeable with a duty of the amount indicated in that Schedule as the proper duty therefor, namely:

- (a) every instrument mentioned in that Schedule which, not having been previously executed by any person, is executed in India on or after the first day of July, 1899;
- (b) every bill of exchange payable otherwise than on demand or promissory note drawn or made out of India on or after the date and accepted or paid, or presented for acceptance or payment, or endorsed, transferred or otherwise negotiated in India; and
- (c) every instrument (other than a bill of exchange or promissory note) mentioned in that Schedule, which, not having been previously executed by any person, is executed out of India on or after that day and relates to any property situate, or to any matter or thing done or to be done in India and is received in India.

However, no duty shall be chargeable in respect of:

1. any instrument executed by or on behalf of or in favour of the Government, in cases where, but for this the Government would be liable to pay the duty chargeable in respect of such instrument.
2. any instrument for the sale, transfer or disposition, either absolutely or by way of mortgage or otherwise, of any ship or vessel or any part, interest, share of property of or in any ship or vessel registered under the Merchant Shipping Act, 1894 or under Act XIX of 1838 or the Indian Registration of Ships Act, 1841 as amended by subsequent Acts.

[The references to repealed Acts are now to be read as references to the corresponding re-enacting Act].

3. Any instrument executed by, or, on behalf of, or in favour of, the Developer or Unit or in connection with the carrying out of purposes of the special Economic Zone.

*Explanation* – For the purposes of this clause, the expressions “Developer” “Special Economic Zone” and “Unit” shall have meanings respectively assigned to them in Clauses (g), (za) and (zc) of Section 2 of the Special Economic Zones Act, 2005.\*

Thus, Section 3 charges certain instruments to be liable to stamp duty.

The Court has observed as under in *Commissioners of Inland Revenue v. G. Angus*, 1889) 23 QBD 579, followed in *re Swadeshi Cotton Mills*, AIR 1932 All 291, “the first thing to be noticed is that thing which is made liable to duty is an instrument. If a contract of purchase and sale or a conveyance by way of purchase and sale, can be, or is carried out without an instrument the case is not within the section and no tax is imposed. It is not the transaction of purchase and sale which is struck at; it is the instrument whereby the purchase and sale are effected which is struck at. And if any one carries through a purchase and sale without an instrument, then the Legislature has not reached that transaction”.

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\* Clause 3 mentioned above has been inserted by the Special Economic Zones Act, 2005.



*In re Swadeshi Cotton Mills*, AIR 1932 All 291, it was held that if after entry into a contract of sale the parties (in spite of the risk that either party may rescile from the contract), refrain from getting an *actual deed of conveyance* prepared, they can successfully evade the payment of higher duty. It is no argument that the Government loses revenue, if such a course is permitted\*\*.

On this point Esher M.R., in *Commissioners of Inland Revenue v. G. Angus*, (1889) 23 QBD 579, stated that “goodwill can be sold and conveyed to purchasers without any ‘conveyance’ being executed and if you treat the document as only an agreement with regard to the goodwill, there will never be any conveyance executed and the property would have been transferred to the purchaser without the Crown getting any *ad valorem* duty upon the transfer. If a vendor can convey the property sold to the purchaser without the execution of any instrument, he can convey it without paying any duty under Section 70. The subject may have the good fortune to escape the stamp duty, if he can get a conveyance of property sold to him without the execution of any instrument..... “The Crown ..... must make out its right to duty and if there be a means of evading the stamp duty, so much the better for those who can evade it”.

### Substance and description

Courts have invariably upheld the principle of substance of the transaction, over the form, in the matter of deciding the nature of the instrument. The substance of the transaction contained in the document may not necessarily embody the description given at the head thereof.

It is the substance of the transaction as contained in the instrument and not the form of the instrument, that determines the stamp duty, though the duty is leviable on the instrument and not on the transaction. In determining whether a document comes within the description of a document upon which a stamp is required by the Act, one has to look at the entire document to find out whether it falls within the description. Where a single instrument contains several purposes, the instrument as a whole should be read to find out its dominant purpose. To determine whether a document is sufficiently stamped the Court must look at the document itself, as it stands.

### EXTENT OF LIABILITY OF INSTRUMENTS TO DUTY (SEVERAL INSTRUMENTS IN SINGLE TRANSACTION OF SALE, MORTGAGE OR SETTLEMENT)

Section 4 provides that, where in the case of any sale, mortgage or settlement, several instruments are employed for completing the transaction –

- only the principal instrument shall be chargeable with the duty prescribed for the conveyance, mortgage or settlement; and
- each of the other instruments shall be chargeable with a duty of one rupee (instead of the duty if any prescribed for the other instruments).

### Illustrations (Section 4 held applicable)

- A executed a conveyance of immovable property. On the same deed his nephew (undivided in status) endorsed his consent to the sale, as such consent was considered to be necessary. It was held that the conveyance was the principal instrument. The consent was chargeable with only one rupee (ILR 13 Bom 281).

\*\* However, in some states, local amendments have imposed heavy duty on agreements for sale.

- (ii) Subsequent to a sale of immovable property, two declarations were executed reciting that the sale was subject to an equitable mortgage created by the vendor. These declarations were held to be chargeable, together with the sale deed, as having completed the conveyance (*Somaiya Organics Ltd. v. Chief Controlling Revenue Authority*, AIR 1972 All 252).
- (iii) Brother *A* executed in favour of brother *B* a gift of all his property. By another deed, brother *B* made provision for the living expenses of brother *A* and hypothecating in favour of brother *A* a part of the property included in the above mentioned gift deed, in order to secure the payment of the living expenses. It was held that the two documents were part of the same transaction. They amounted to a settlement and Section 4 applied (*Maharaj Someshwar Dutt*, ILR 37 All 264).
- (iv) *B* conveyed the whole of his property to three persons who undertook to provide for him and to perform his obsequies. By another document, the three donees agreed to provide for *B*. This was mentioned in the deed executed by *A* also. It was held that the two documents had to be construed as part of the same act; the first was liable to duty as a conveyance while the second was liable to a duty of Rupee 1 only (*Dadoba v. Krishna*, ILR 7 Bom. 34).
- (v) A company executed, first a deed of trust and mortgage stating that the company was to issue notes for raising loans secured by the sale deed. It was held as under:
  - (1) The deed was principal or primary security (and not a collateral security). It was chargeable as mortgage under Article 14.
  - (2) **The notes issued subsequently were debentures and not principal instruments (*Madras Refinery Ltd. v. Chief Controlling Revenue Authority, Madras*, AIR 1977 SC 500).**
- (vi) The Rangoon Gymkhana executed a duly stamped trust deed, mortgaging its assets as security for the repayment of the debenture stock issued by it. In addition, it had issued certificates of debenture stock to the subscribers, but these did not contain any promise to repay any need, but merely stated the amount standing in each stock holder's name. It was held that the certificates were not debentures, but were instruments employed to complete the mortgage [*Rangoon Gymkhana In re*, AIR 1927 Rang. 37 (Section 4 applied)].

#### SECTION 4 NOT APPLICABLE

- (i) A lease is executed and got registered. A second document is executed altering the terms of the first document. The second document has to be stamped as a lease. Section 4 does not apply.
- (ii) A purchaser of land executes a mortgage of the land in favour of the vendor for a portion of the purchase money. The mortgage is liable to full duty as a separate instrument. Section 4 does not apply.

#### Instruments relating to several distinct matters

Under Section 5, an instrument comprising or relating to several distinct matters is chargeable with the aggregate amount of the duties with which each separate instrument, relating to one of such matters, would be chargeable under the Act (This is the reverse of the situation governed by Section 4).

The Section deals with multifarious instruments. The expression "distinct matter" means distinct transactions (*Ram Swarup v. Joti*, (1933) Allahabad Law Journal 427; *Board of Revenue, Madras v. Narasimhan*, AIR 1961 Mad 504).

Section 5 applies even where the two (or more) matters are of the same description.

### Illustrations as to “distinct matters”

- (i) A document containing both an agreement for the dissolution of a partnership and a bond, is chargeable with the aggregate of the duties with which two such separate instruments would be chargeable. The two are “distinct matters” (*Chinmoyee Basu v. Sankare Prasad Singh*, AIR 1955 Cal. 561 (cf. AIR 1936 Lah. 449)).
- (ii) **An agreement containing two covenants making certain properties chargeable in the first instance and creating a charge over certain properties if the first mentioned properties are found insufficient does not fall within Section 5 (*Tek Ram v. Maqbul Shah*, AIR 1928 Lah. 370).**
- (iii) A grant of annuity by several persons requires only one stamp (because there is only one transaction).
- (iv) A lease to joint tenants requires only one stamp.
- (v) A conveyance by several persons jointly relating to their separate interest in certain shares in an incorporated company requires only one stamp.
- (vi) A power of attorney executed by several persons authorising the agent to do similar acts for them in relation to different subject matter is chargeable under Section 5, where they have no common interest.
- (vii) Where a person having a representative capacity (as a trustee) and a personal capacity delegates his powers in both the capacities, section 5 applies. In law, a person acting as a trustee is a different entity from the same person acting in his personal capacity.
- (viii) **The position is the same where a person is an executive or administrator and signs an instrument containing a disposition by him in his personal capacity and also a disposition as executor. The two capacities are different (*Member, Board of Revenue v. Archur Paul Bentall*, AIR 1956 SC 35).**

### Principal and ancillary

The test is – “What is the leading object? Which is principal and which is ancillary?

If an instrument taken with reference to its primary object is exempted then stamp duty cannot be charged merely because matter ancillary to it is included and that matter is chargeable to stamp duty. A very common example of this is an agreement for sale of goods, which also contains an arbitration clause. The latter clause is incidental to the former agreement. Where a deed of dissolution of partnership contains a clause charging the partnership assets for payment of certain amounts to outgoing parties, the instrument is chargeable separately for the charge and the partnership. The former is not ancillary to the latter.

Where a document contains a transfer of mortgage and *an agreement* to make a loan, the mortgage and the loan are distinct matters and separately chargeable.

If in a lease there is also an agreement to pay a certain sum on account of the balance of previous year, the document is chargeable (i) as a lease and (ii) also as a bond.

A lease reserving *separately* rent for house and rent for furniture is chargeable separately for each of the items.

Where, at an auction, a purchaser purchases several lots and there is only one instrument in respect of all of them the separate purchases are, nevertheless, separate and distinct matters and so, the stamp duty must be determined separately.

Thus, the test usually adopted is the test of “leading object”. If there is only one leading object, Section 5 will not apply. But if there are several distinct contracts, each is taxable.

### **INSTRUMENTS COMING WITHIN SEVERAL DESCRIPTIONS IN SCHEDULE-I**

There may be cases where an instrument may come under several descriptions in Schedule-I to the Act. In such a circumstance, Section 6 of the Act provides that the instrument shall, where the duties chargeable thereunder are different, be chargeable only with the highest of such duties. Section 6 is subject to the provisions of Section 5. However, nothing in the Act shall render chargeable, with duty exceeding one rupee, a counter part or duplicate, of any instrument chargeable with duty, in respect of which the proper duty has been paid.

Section 6 applies only where the instrument contains only one matter, but falls within two or more items in the Schedule. Section 6 covers cases where the instrument does not cover distinct matters but is ambiguous in regard to the various entries given in Schedule-I to the Act. In such cases, Section 6 clearly provides that the highest of the duties mentioned against the various descriptions against which the instrument is likely to fall is to be paid.

Where a deed (I) contains a stipulation binding the executant to deliver his sugarcane crop to the obligee under the deed and (ii) also provides that the sugarcane crop is hypothecated as security for payment of money advanced by the obligee, the deed fulfills the dual character of the mortgage and a bond and is therefore chargeable to the highest of the duties by virtue of section 6. Similarly, where an attested instrument, containing an undertaking to pay money, evidences also a pledge of immovable property as security for the money due, the higher of the stamp duty payable on its character as a bond and on its character as a pledge, was held leviable. An instrument which can be treated both as a dissolution of partnership and as an instrument of partition has to be charged to the duty prescribed for partition deed, which is the higher of the two.

### **BONDS, DEBENTURES, ETC. ISSUED UNDER THE LOCAL AUTHORITIES LOAN ACT, 1879**

Section 8 provides that any local authority raising a loan under the provisions of the Local Authorities Loans Act, 1879 or of any other law for the time being in force by the issue of bonds, debentures or other securities, shall, in respect of such loans, be chargeable with a duty of one percent on the total amount of the bonds, debentures or other securities issued by it. Such bonds, debentures or other securities need not be stamped and shall not be chargeable with any further duty on renewal, consolidation, sub-division or otherwise. This is so notwithstanding anything contained in the Indian Stamp Act: In the event of willful neglect to pay the duty required by this section, the local authority shall be liable to forfeit to the Government, a sum equal to 10 percent of the amount of duty payable and a like penalty for every month after the first, during which the neglect continues.

### **SECURITIES DEALT IN DEPOSITORY NOT LIABLE TO STAMP DUTY**

As per Section 8A of the Act—

- (a) an issuer, by the issue of securities to one or more depositories shall, in respect of such issue, be chargeable with duty on the total amount of security issued by it and such securities need not be stamped;
- (b) where an issuer issues certificate of security under sub-section (3) of Section 14 of the Depositories Act, 1996, on such certificate duty shall be payable as is payable on the issue of duplicate certificate under this Act;

- (c) the transfer of—
  - (i) registered ownership of securities from a person to a depository or from a depository to a beneficial owner;
  - (ii) beneficial ownership of securities, dealt with by a depository;
  - (iii) beneficial ownership of units, such units being units of a Mutual Fund including units of the Unit Trust of India established under sub-section (1) of Section 3 of the Unit Trust of India Act, 1963, dealt with by a depository,

shall not be liable to duty under this Act or any other law for the time being in force.

*Explanation 1* – For the purposes of this section, the expressions “beneficial ownership”, “depository” and “issuer” shall have the meanings respectively assigned to them in clauses (a), (e) and (f) of Sub-section (1) of Section 2 of the Depositories Act, 1996.

*Explanation 2* – For the purposes of this section, the expression “securities” shall have the meaning assigned to it in clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956.

### CORPORATISATION AND DEMUTUALISATION SCHEMES AND RELATED INSTRUMENTS NOT LIABLE TO DUTY

Section 8B has been inserted by the Finance Act, 2005, w.e.f. 13.5.2005. Section 8B states that

- (a) a scheme for corporatisation or demutualisation, or both of a recognized stock exchange; or
- (b) any instrument, including an instrument of, or relating to, transfer of any property, business, asset whether movable or immovable, contract, right, liability and obligation, for the purpose of, or in connection with, the corporatisation or demutualisation, or both of a recognized stock exchange pursuant to a scheme,

as approved by the Securities and Exchange Board of India under Sub-section (2) of Section 4B of the Securities Contracts (Regulation) Act, 1956 shall not be liable to duty under this Act or any other law for the time being in force.

*Explanation* — For the purposes of this Section—

- (a) the expressions “corporatisation”, “demutualisation” and “scheme” shall have the meanings respectively assigned to them in clauses (aa), (ab) and (ga) of Section 2 of the Securities Contracts (Regulation) Act, 1956;
- (b) “Securities and Exchange Board of India” means the Securities and Exchange Board of India established under Section 3 of the Securities and Exchange Board of India Act, 1992.

#### ***Test your knowledge***

##### ***Choose the correct answer***

*Which of the following sections deals with multifarious instruments?*

- (a) Section 4
- (b) Section 70
- (c) Section 3
- (d) Section 5

***Correct answer: (d)***



## REDUCTION, REMISSION AND COMPOUNDING OF DUTIES

Section 9 empowers the Government, (Central or the State as the case may be), to reduce or remit, whether prospectively, or retrospectively, the duties payable on any instrument or class of instruments or in favour of particular class of persons or members of such class. Section 9 also empowers the Central Government to provide for the composition or consolidation of duties of policies of insurance and in the case of issues by any incorporated company or other body corporate or of transfers where there is single transferee (whether incorporated or not) of debentures, bonds or other marketable securities.

## VALUATION FOR DUTY UNDER THE ACT

Sections 20 to 28 (Chapter II of the Act) deal with valuation of instruments for duty.

- (a) According to Section 20, where an instrument is chargeable with *ad valorem* duty in respect of any money expressed in any currency other than that of India, such duty shall be calculated on the value of such money in the currency of India, according to the current rate of exchange on the date of the instrument. The Central Government notifies from time to time, in the Official Gazette the rate of exchange for conversion of certain foreign currencies into Indian currency for this purpose and such rate shall be deemed to be the current rate.
- (b) Section 21 provides that in the case of an instrument chargeable with *ad valorem* duty in respect of any stock or any marketable or other security, such duty shall be calculated on the value of such stock or security according to the average price or the value thereof on the date of the instrument. The term "marketable security" has been defined in Section 2(16-A) of the Act.

Where the shares are quoted on the stock exchange, it is easy to ascertain the price of the shares or stock. However, where the shares or stocks are not quoted on any stock exchange, the valuation has to be based upon the average of the latest private transactions, which can generally be ascertained from the principal officer of the concerned company or corporation. If, there have been no dealings at all, then unless some other reliable evidence of market value is forthcoming the value is to be taken at par. Section 22 of the Act, however, provides that if such price or value is mentioned in the instrument for the purpose of calculating duty, it shall be presumed (until the contrary is proved) to be correct.

- (c) Section 23 provides that where interest is expressly made payable by the terms of the instrument, such instrument shall not be chargeable with a duty higher than that with which it would have been chargeable, had no mention of interest been made therein. For instance, a promissory note for Rs. 10,000 is drawn with the recital of interest at the rate of 18 percent per annum, payable by the promisor; stamp is leviable on the basis that the instrument is for Rs. 10,000 only.
- (d) Section 23A provides that in the case of an instrument (not being a promissory note or bill of exchange) which -
  - (i) is given upon the occasion of the deposit of any marketable security by way of security for money advanced or to be advanced by way of loan, or for an existing or future debt, or
  - (ii) makes redeemable or qualifies a duly stamped transfer, intended as a security, of any marketable security.

It shall be chargeable with duty as if it were an agreement or memorandum of an agreement, chargeable with duty under Article 5(c) of Schedule I to the Act.

- (e) A release or discharge of any such instrument shall be chargeable only with the like duty.

- (f) According to Section 24, where any property is transferred to any person in consideration (wholly or in part) of any debt due to him, or subject either certainly or contingently to the payment or transfer of any money or stock, (whether being or constituting a charge or incumbrance upon the property or not), such debt, money or stock is to be deemed the whole or part, (as the case may be), of the consideration in respect whereof the transfer is chargeable with *ad valorem* duty. However, nothing in this section shall affect such a certificate of sale as is mentioned in Article 18 of the First Schedule to the Act.

The object of this section is that, upon every purchase *ad valorem* duty has to be paid on the entire consideration which either directly or indirectly represents the value of the free and unencumbered corpus of the subject matter of the sale (*Collector of Ahmedabad v. Deepak Textile Industries*, AIR 1966 Guj. 227).

What Section 24 means is that where property is sold subject to the payment by the purchaser, discharging a debt charged on the property, then the purchaser is really paying a consideration which includes the amount of that debt also (*Somayya Organics Ltd. v. Board of Revenue*, AIR 1986 SC 403).

Proviso to Section 24 operates for the benefit of assignee of the mortgage.

When the mortgaged property is sold to the mortgagee along with other properties, the stamp duty already paid is to be deducted from the duty payable on the deed of sale. In order to entitle the mortgagee to a deduction of the duties payable the entire property mortgaged should be transferred and not merely a portion of it (*In re Mirabai, in re Laxman and Ganpat*, ILR 29 Bom. 203).

Explanation to Section 24 provides that in the case of sale of property subject to mortgage or other encumbrances, any unpaid mortgage money or money charged together with the interest, if any, due on the same shall be deemed to be part of the consideration for the sale provided that where property subject to a mortgage is transferred to the mortgagee he shall be entitled to deduct from the duty payable on the transfer the amount of any duty already paid in respect of the mortgage. Three illustrations which have been appended to the Section are as under:

- (i) A owes B Rs. 1,000/-. A sells a property to B, the consideration being Rs. 500/- and the release of the previous debt of Rs. 1,000/-. Stamp duty is payable on Rs. 1,500/-
  - (ii) A sells a property to B for Rs. 500 which is subject to a mortgage to C for Rs. 1,000/- and unpaid interest Rs. 200/-. Stamp duty is payable on 1,700.
  - (iii) A mortgages a house of the value of Rs. 10,000/- to B for Rs. 5,000/-. B afterwards buys the house from A. Stamp duty is payable on Rs. 10,000/- less the amount of stamp duty already paid for the mortgage.
- (g) Section 25 deals with the manner of computation of duty in the case of annuities. Valuation of an annuity will be material, where the payment of annuity or other sum payable periodically is secured by an instrument or where the consideration for a conveyance is an annuity or other sum payable periodically. In such cases, the amount secured by such instrument or the consideration for such conveyance, as the case may be, shall be deemed to be:
- (i) where the sum payable is for a definite period so that the total amount to be paid can be previously ascertained such total amount;
  - (ii) where the sum is payable in perpetuity or for an indefinite time not terminable with any life in being at the date of such instrument or conveyance – the total amount which, according to the terms of such instrument or conveyance will or may be payable during the period of twenty years calculated from the date on which the first payment becomes due, and

- (iii) where the sum is payable for an indefinite time terminable with any life in being at the date of such instrument or conveyance – the maximum amount which will be or which may be payable as aforesaid during the period of 12 years calculated from the date on which the first payment becomes due.

Clause (a) mentioned above applies where the sum is payable for a definite period, so that the total amount to be paid can be previously ascertained. According to clause (b), where the payment is in perpetuity or for an indefinite period, then only the amount payable for 20 years would be taken for assessment of the duty.

### **Illustration**

By a document, 'A' binds himself and his posterity on the security of some immovable property for the annual payment to a temple of Rs. 2,200/- It is a mortgage deed, chargeable with duty calculated on 20 years' payment.

- (h) Section 26 deals with cases where the value of the subject matter is indeterminate. The object of this section is to protect the revenue, in cases where an instrument is chargeable with *ad valorem* duty, but such duty cannot be ascertained by reason of the fact that the amount of value of the subject matter of the instrument cannot be determined at the time of the execution of the instrument. This object is sought to be achieved by providing, that the executant can value the instrument as he pleases, but he shall not be entitled to recover under such document any amount in excess of the amount for which the stamp duty is sufficient.

However, under the combined operation of Sections 26 and 35, a lessee under the mining lease is entitled, upon payment of the proper penalty, to recover the royalty provided for in the stamp originally affixed to the lease. [AIR 1924 PC 221; AIR 1930 Cal. 526]. Section 26 applies only when the instrument is chargeable with *ad valorem* duty. Section 26 has two provisos. Under the first proviso, in the case of mining lease, the stamp duty is to be calculated on the estimated value of the royalty or the share of the produce, as the case may be. If the lease is granted by the Government, stamp duty has to be paid on the amount or value of the royalty as determined by the Collector of Stamps. And, if subsequently any excess is claimed, proper penalty under section 35 may be paid and the claim fully recovered. But when the lease has been granted by a person other than the Government, the valuation has to be at Rs. 20,000/- a year.

The second proviso to Section 26 is intended to cover the case where an instrument has, by accident or mistake, been insufficiently stamped. The deficiency is made up in proceedings under Section 31 or 41 and the Collector having certified the amount paid, it shall be deemed to be the stamp actually used at the date of execution. By reason of this proviso, the amount claimable under the instruments would be the amount for which the duty as certified by the Collector had been paid and not the amount for which duty was originally paid.

### **CONSIDERATION TO BE SET OUT**

Section 27 provides that the consideration and all other facts and circumstances affecting the chargeability of any instrument with duty or the amount of duty with which it is chargeable shall be fully and truly set forth in the instrument. "Value of any property" would mean that real value of the property in the open market at the time the document was executed and not at the time when the executant acquired it. Where there is no value set forth in the instruments, there would be contravention of Section 27, but the omission does not render the document inadmissible or liable to be impounded and taxed in the manner provided in Section 35 (*Vinayak v. Hasan Ali*, AIR 1961 MP 6).



**The Collector cannot proceed to ascertain the value of the property with a view to causing the instrument to be stamped with reference to the value so ascertained by the Collector. The Act does not provide for any powers to the revenue authority to make an independent enquiry into the value of the property conveyed for determining the duty chargeable. (AIR 1922 All 82)**

However, the Collector can direct the prosecution of a person who executed the instrument under Section 64 of the Act. Under Section 64, what is punishable is the omission to set-forth fully and truly the value of the property, with intent to defraud the Government. The Collector, can, if he feels that there is a deliberate under-valuation of property, hold an independent enquiry to ascertain the true value of the property and to consider whether there was deliberate under-valuation rendering the executant liable to prosecution for defrauding the Government.<sup>1</sup>

## APPORTIONMENT

Section 28 prescribes certain rules for apportionment of the consideration, in cases of certain conveyances arising out of a property being contracted to be sold and thereafter conveyed in parts etc.

Under Section 28(1) where a person contracts the sale of property as a *whole* and thereafter conveys to the purchaser the property *in separate parts*, the consideration shall be apportioned in such manner as the parties think fit, provided that a distinct consideration is set-forth for each separate part in the conveyance and thereafter the conveyances shall be chargeable with *ad valorem* in respect of such distinct consideration.

Under Section 28(2), where the contract is for the sale of a property as a whole to two or more purchasers jointly or by any person for himself and others, and the property is conveyed to them *in parts* by separate conveyance, then each distinct part of the consideration shall be chargeable with *ad valorem* duty in respect of the distinct part of the consideration so specified.

Section 28(3) covers cases where a person, after contracting to purchase a property from another and before the property has been duly conveyed to him, enters into a contract to sell the property to a third person, and the contract is given effect to only by one conveyance from the owner of the property to the sub-purchaser directly. The stamp duty payable is on the consideration paid by the sub-purchaser. This provision avoids double payment that would otherwise arise.

Section 28(4) provides that where a person contracts for the sale of property and before obtaining a conveyance in his favour, enters into a contract to sell the property in parts to other persons, the conveyances which may be executed directly by the owner to each sub-purchaser would be liable to be charged with duty in respect of the consideration paid by the sub-purchaser, original price for the whole and the aggregate price paid by the sub-purchasers, subject to a minimum duty of Re. 1/-.

Section 28(5) provides that when a person contracts to sell a property to another person and again contracts to sell the same property to a third person and such third person obtains a conveyance first from the seller with whom he had contracted and later gets another conveyance of the same property from original seller, the duty is to be charged on the consideration received by the original seller subject to a maximum of Rs. 5/-.

## PERSONS LIABLE TO PAY DUTY

Section 29 deals with the persons responsible for payment of duty. Under this section, in the absence of an agreement to the contrary, the expense of providing the proper stamp shall be borne:

<sup>1</sup> In some States, local amendments have given such powers to the collector.

- (a) in the case of any instrument described in any of the following articles of Schedule-I, namely, -
- No. 2 (Administration Bond),
  - No. 6 (Agreement relating to Deposit of Title-deeds, Pawn or Pledge),
  - No. 13 (Bill of Exchange),
  - No. 15 (Bond),
  - No. 16 (Bottomry Bond),
  - No. 26 (Customs Bond),
  - No. 27 (Debenture),
  - No. 32 (Further Charge),
  - No. 34 (Indemnity-bond),
  - No. 40 (Mortgage-deed),
  - No. 49 (Promissory-note),
  - No. 55 (Release),
  - No. 56 (Respondentia Bond),
  - No. 57 (Security Bond or Mortgage-deed),
  - No. 58 (Settlement),
  - No. 62(a) (Transfer of shares, in an incorporated company or other body corporate),
  - No. 62(b) (Transfer of debentures, being marketable securities, whether the debenture is liable to duty or not, except debentures provided for by Section 8),
  - No. 62(c) (Transfer of any interest secured by a bond, mortgage-deed or policy of insurance), -  
by the person drawing, making or executing such instrument;
- (b) in the case of a policy of insurance other than fire insurance by the person effecting the insurance;
- (c) in the case of a policy of fire-insurance – by the person issuing the policy;
- (d) in the case of a conveyance including a reconveyance of mortgaged property by the grantee; in the case of a lease or agreement to lease by the lessee or intended lessee;
- (e) in the case of a counterpart of a lease – by the lessor;
- (f) in the case of an instrument of exchange – by the parties in equal shares;
- (g) in the case of a certificate of sale – by the purchaser of the property to which such certificate relates; and
- (h) in the case of an instrument of partition – by the parties thereto in proportion to their respective shares in the whole property partitioned, or, when the partition is made in execution of an order passed by a Revenue Authority or Civil Court or arbitrator, in such proportion as such authority, Court or arbitrator directs.

## RECEIPTS

Under Section 30 of the Act any person receiving any money exceeding twenty rupees in amount or any bill of exchange, cheque or promissory note for an amount exceeding five hundred rupees or receiving in satisfaction of a debt any movable property exceeding five hundred rupees in value, shall on demand by the person paying or delivering such money, bill, cheque, note, or property, give a duly stamped receipt for the same.

## PARTY LIABLE TO PAY

Section 29 specifies in the case of certain instruments which party should pay, for the stamp. The section is not exhaustive and makes no reference to several instruments. Section 30 contains a special provision as to stamping of receipts. There are several other instruments not mentioned in Section 29, for which there is no express provision as to who should bear the stamp expenses. The primary duty of stamping lies in all cases on the person executing the instrument as Section 17 directs that the instruments chargeable with duty shall be stamped at or before executing an instrument without the same being duly stamped. Section 29 would apply only in the absence of a special agreement between the parties as stated in the opening words of the section. An agreement to bear the cost of preparation of an instrument implies an agreement to pay stamp duty also on it.

Any person receiving or taking credit for any premium or consideration for any renewal of any contract of fire-insurance, shall, within one month after receiving or taking credit for such premium or consideration, give a duly stamped receipt for the same.

## METHODS OF STAMPING

- (a) According to the provisions of the Act and rules made thereunder, the duty with which an instrument is chargeable is to be paid by means of stamps indicated in the Act and the rules. Generally, rules deal with the subject.

Section 10 provides that all duties with which any instrument is chargeable shall be paid, and such payment shall be indicated on such instrument, by means of stamps according to the provisions contained in the Act, or when no such provision is applicable thereto, as the State Government concerned may by rule, direct. The rules may, among other matters, regulate:

- (i) in the case of each kind of instrument, the description of stamps which may be used;
  - (ii) in the case of instruments stamped with impressed stamps, the number of stamps which may be used;
  - (iii) in the case of bills of exchange or promissory notes, the size of the paper on which they are written.
- (b) There are two types of stamping, namely:
- (i) Adhesive stamping, and
  - (ii) Impressed stamping.

## USE OF ADHESIVE STAMPS

Section 11 deals with the *use of adhesive stamps*. This Section provides that the following instruments may be stamped with adhesive stamps, namely –

- (a) instruments chargeable with a duty not exceeding 10 naya paisa except parts of bills of exchange payable otherwise than on demand and drawn in sets;
- (b) bills of exchange and promissory notes drawn or made out of India;
- (c) entry as an advocate, vakil or attorney on the roll of a High Court;
- (d) notarial acts; and
- (e) transfers by endorsement of shares in any incorporated company or other body corporate.

The use of the words 'may be stamped' really connotes 'shall be stamped'. The rules framed under the Stamp Act as well as under the relevant state laws invariably provide that the adhesive stamps shall carry special words, to indicate the use to which the stamps can be put.

### CANCELLATION OF ADHESIVE STAMPS

Section 12(1)(a) provides that any person affixing any adhesive stamp to any instrument chargeable with duty which has been executed by another person shall, when affixing such stamp cancel the same so that it cannot be used again. Under Sub-section (1)(b), an obligation has been imposed on person executing any instrument on any paper bearing an adhesive stamp, to cancel the stamp, if such cancellation has not been done, at the time of such execution. If a person fails to cancel the stamp, he becomes liable to penalty in accordance with Section 63. The object is to prevent the same stamp from being used again.

Under Sub-section (2) of Section 12, any instrument bearing an adhesive stamp which has not been cancelled is deemed to be unstamped.

### MODE OF CANCELLATION OF ADHESIVE STAMPS

- (a) Section 12(3) deals with the mode of cancellation of stamp. It provides that the cancellation of an adhesive stamp may be done by the person concerned by writing on or across the stamp his name or initials, or the name or initials of his firm with the true date of his so writing, or in any other *effectual manner*. Sub-section (3) merely lays down as a guidance one of the ways in which an adhesive stamp can be cancelled.
- (b) In *Mahadeo Koeri v. Sheoraj Ram Teli*, ILR 41 All 169; AIR 1919 All 196, it was held that a stamp may be treated as having been effectively cancelled by merely drawing a line across it.

But, in *Hafiz Allah Baksh v. Dost Mohammed*, AIR 1935 Lah. 716, it was held that if it is possible to use a stamp a second time, in spite of a line being drawn across it, there is no effectual cancellation. Again, the question whether an adhesive stamp has been cancelled in an effectual manner has to be determined with reference to the facts and circumstances of each case.

In *Melaram v. Brij Lal*, AIR 1920 Lah. 374, it was held that a very effective method of cancellation is the drawing of diagonal lines right across the stamps with ends extending on to the paper of the document. A cross marked by an illiterate person indicating his acknowledgement, was held to be an effective cancellation of the stamp in *Kolai Sai v. Balai Hajam*, AIR 1925 Rang. 209. Accordingly, where the adhesive stamps on promissory note were cancelled by drawing lines on them in different directions and stretching beyond the edge of the stamp on the paper on which the promissory note was written, it was held that the stamp had been effectually cancelled. Where one of the four stamps used on an instrument had a single line drawn across the face of the stamp, the second had two parallel lines, the third three parallel lines and the fourth two lines crossing each other, it was held that the stamps must be regarded as having been cancelled in manner so that they could not be used again (*In re Tata Iron Steel Company*, AIR 1928 Bom. 80). Putting two lines crossing each other is effective (AIR 1961 Raj. 43).

- (c) However, putting a date across the stamp by a third party *on a date subsequent to the date on which the bill had been drawn*, was held to be not proper cancellation in *Daya Ram v. Chandu Lal*, AIR 1925 Bom. 520 Cf. *Rohini v. Fernandes*, AIR 1956 Bom. 421, 423. Similarly, crossing by drawing lines and signing on the adjacent stamp was held to be not a cancellation of the first stamp in *U. Kyaw v. Hari Dutt*, AIR 1934 Rang. 364. Cross is a good way of cancellation. AIR 1976 Cal. 99.

- (d) Where it is alleged that the cancellation was made at later stage than that of execution, the burden of proving it, lies on the party who so alleges. Where an instrument *prima facie* appears to be duly stamped and cancelled by the drawer at the date of execution, the burden of proving the contrary lies on the party who avers that the cancellation was not effected at the time of execution. In the absence of evidence to the contrary, it may be inferred that the stamp was duly affixed and cancelled.

### **Instruments Stamped with Impressed Stamps how to be Written (Writing on Stamp Paper)**

- (a) Section 13 provides that every instrument written upon paper stamped with an *impressed stamp* shall be written in such manner that the stamp may appear on the face of the instrument and cannot be used for or applied to any other instrument. The expression, 'face of the instrument' is not to be interpreted as meaning that the document must commence on the side on which the stamp is impressed or that both sides of the paper or parchment may not be written upon. In *Dowlat Ram Harji v. Vitho Radhoji*, 5 Bom. 188, it was held when the face of a deed or document is mentioned, no particular side of the parchment or paper, on which the deed or document is written, is thereby indicated. Even the last line may constitute the face (Westroph, CJ.).
- (b) Under Section 14, no second instrument chargeable with duty shall be written upon piece of stamp paper upon which an instrument chargeable with duty has already been written. However, this section shall not prevent any endorsement which is duly stamped or is not chargeable with duty, being made upon any instrument for the purpose of transferring any right created or evidenced thereby, or of getting the receipt of any money or goods the payment or delivery of which, is secured thereby.
- (c) The object of Section 14 is to prevent a stamped paper which has been used for one instrument, from being used for another instrument thereby avoiding payment of duty in respect of second instrument, AIR 1928 Rang 262. Except for an endorsement of the kind referred to earlier, no second instrument shall be engrossed on a stamp paper on which there is already written 'an instrument chargeable with duty'.

An alteration in the instrument as originally written, if it is of such nature, as to require fresh stamp, would come within the prohibition contained in the section. It is an important question as to what would be a material alteration<sup>1</sup> which converts an instrument written on stamp paper into a second instrument within the meaning of Section 14. A "material alteration" is one which alters (or purports to alter), the character of the instrument itself and which affects (or may affect) the contract which the instrument contains or alters evidence of any charge, or varies the liability under the instrument in any way. An alteration which vitiates the instrument as could cause it to operate differently was also held to be a material alteration. An alteration which *may affect the contract* which the instrument contains is a material alteration.

Section 15 of the Act deems every instrument written in contravention of Section 13 or Section 14 to be unstamped and to be inadmissible in evidence as not being duly stamped.

### **DENOTING DUTY**

Section 16 of the Act deals with denoting duty. The object of this section is to spare parties to an instrument, the inconvenience of having to produce (in cases in which the duty payable on an instrument depends upon the duty already paid on another instrument), the original or principal instrument in order to prove that the second instrument has been duly stamped. Section 16 provides that where the duty with which an instrument

<sup>1</sup> (1905) ILR 33 Cal 812: ILR 14 Rang 29.

is chargeable, or its exemption from duty, depends in any manner upon the duty actually paid in respect of another instrument, the payment of such last mentioned duty, shall, if application is made in writing to the Collector for that purpose, and on production of both the instruments, *be denoted upon such first mentioned instrument*, by endorsement under the hand of the Collector of Stamps or in such other manner as the rules of the State Government may provide.

### TIME OF STAMPING INSTRUMENTS

(a) *Instruments executed inside India:* Section 17 provides that all instruments chargeable with duty and executed by any person in India shall be stamped before or at the time of execution. The scope of Section 17 is restricted to only instruments executed in India. If the executant of a document has already completed the execution of the document and in the eye of law the document, could be said to have been executed, a subsequent stamping, (however close in time) could not render the document as one stamped at the time of execution. Thus, where a promissory note is executed by 'A' and 'B' and a stamp is afterwards affixed and cancelled by 'A' by again signing it, the stamping has taken place subsequent to the execution and hence, the provisions of Section 17 are not complied with (*Rohini v. Fernandes*, AIR 1956 Bom 421). A receipt stamped subsequent to its execution, but before being produced in the Court is not stamped in time and accordingly, not admissible in evidence.

(b) *Instruments executed outside India:* Section 18 relates to foreign instruments (other than bills and notes), received in India; Foreign bills and notes received in India have been dealt with, in Section 19. According to Section 18, every instrument chargeable with duty executed only out of India and (not being a bill of exchange or promissory note) *may be stamped* within three months after it has been first received in India. Section 18(2) provides that where such instrument cannot with reference to the description of stamp prescribed therefor, be duly stamped by a private person, it may be taken within the said period of three months to the Collector who shall stamp the same in such a manner as the State Government may by rule prescribe, with a stamp of that value as the person so taking such instrument may require and pay for. Where an instrument is brought to the Collector after the expiry of three months, the Collector may, instead of declining to stamp it, validate it under Sections 41 and 42 if he is satisfied that the omission to stamp in time was due to a reasonable cause.



The object of Section 18 is to facilitate the stamping of the documents within a period of three months, in as much as, by the very nature of things, Section 17 relating to instruments executed in India cannot be complied with. Section 18 is intended to mitigate the inconvenience and hardship that will entail if the instrument concerned is required to be stamped before or at the time of execution as laid down in Section 17. Instrument executed in India is not within Section 18 (*Nath Bank v. Andhar Mamik Tea Co.*, AIR 1960 Cal 779).

As far as bills of exchange and promissory notes are concerned, Section 19 makes an elaborate provision. Any bill of exchange payable otherwise than on demand or promissory note drawn or made out of India must be stamped and the stamp cancelled, before the first holder in India deals with the instrument, i.e., presents the same for acceptance or payment, or endorses transfers or otherwise negotiates the same in India.

The proviso to Section 19 clarifies that if, (i) at any time any bill of exchange or note comes into the hands of any holder thereof in India, (ii) the proper adhesive stamp is affixed thereto and cancelled in the manner prescribed by Section 12 and (iii) such holder has no reason to believe that such stamp was affixed or cancelled otherwise than by the person, and at the time required by the Act, then such stamp shall (so far as relates to such holder), be deemed to have been duly affixed and cancelled. However, nothing contained in the proviso shall relieve any person from any penalty incurred by him, for omitting to affix or cancel a stamp.

## ADJUDICATION AS TO STAMPS

(a) Chapter III, consisting of Sections 31 and 32, deals with adjudication by the Collector, as to the proper stamp that an instrument has to bear. The provisions of this Chapter are intended to assist any party who is in doubt as to the proper stamp to be affixed on an instrument but is nevertheless anxious to stamp the instrument. When the document or any draft of the document is produced to the Collector he shall determine the proper stamp duty on payment of a nominal fee. The relevant provisions of the Act and matters in regard to the performance of this function by the Collector are discussed below.

(b) Under Section 31(1) when (i) an instrument, (whether executed or not and whether previously stamped or not), is brought to the Collector, and (ii) the person bringing it applies to have the opinion of that officer as to the duty if any, with which it is chargeable, and (iii) pays a fee (not exceeding Rs. 5 and not less than 50 naya paise as the Collector may direct), the Collector shall determine the duty if any with which in his judgment, the instrument is chargeable. Under Section 31 (2), the Collector may require to be furnished with an abstract of the instrument and also with such affidavit or other evidence as he may deem necessary to prove that all the facts and circumstances affecting the chargeability of the instrument with duty, or the amount of duty with which it is chargeable, are fully and truly set-forth therein, and may refuse to proceed upon accordingly. However, no evidence furnished pursuant to this section shall be used against any person in any civil proceeding, except in an enquiry as to the duty with which the instrument to which it relates is chargeable. Every person by whom such evidence is furnished shall, on payment of the full duty, be relieved from any penalty which he may have incurred under the Act by reason of the omission to state truly in such instrument any of the facts or circumstances.

(c) The duty of the Collector under Section 31 is only to determine the stamp duty payable upon the instrument. He is not authorised to impound the instrument or to impose any penalty if he comes to the conclusion that the instrument is not sufficiently stamped. Where a person has obtained the opinion of the Collector on any *draft instrument*, and thereafter does not want to proceed any further to execute the instrument, no consequences will follow and, after determination of the duty, the Collector becomes *functus officio*. But where the party wants to *proceed with effectuating* the instrument or using it for the purposes of evidence, he has to pay the duty determined by the Collector and obtain from the Collector under Section 32, an endorsement that the full duty with which the instrument is chargeable has been paid. Normally, the determination by the Collector of the duty payable on an instrument under Section 31 is final.

(d) Section 32 deals with certificate by the Collector of Stamps as well as the time limit within which such a certificate can be given by the Collector of Stamps. Sub-section (1) of the section provides that when an instrument is brought to the Collector with an application for having an opinion as to the proper duty chargeable thereon, and the Collector is of the opinion that the instrument is already fully stamped or the duty determined by the Collector under Section 31 or such a sum as (with the duty already paid in respect of the instrument), is equal to the duty so determined, has been paid, the Collector shall certify by endorsement on such instrument, that the full duty (stating the amount) with which it is chargeable has been paid. When the Collector is of opinion that any such instrument brought to him is not chargeable with duty, he shall certify in the same manner that such instrument is not so chargeable. Under Section 32(3), any instrument upon which an endorsement has been made by the Collector shall be deemed to be duly stamped or not chargeable with duty as the case may be, and if chargeable with duty, shall be receivable in evidence or otherwise and may be acted upon and registered as if it had been originally duly stamped.

The proviso to Section 32(3) categorically provides that the Collector shall not make any endorsement on any instrument under Section 32, where –

- (a) any instrument is executed or first executed in India and brought to him after the expiration of one month from the date of its execution or first execution, as the case may be;

- (b) any instrument is executed or first executed out of India and brought to him after the expiration of three months after it has been first received in India; or
- (c) any instrument chargeable with a duty not exceeding 10 naya paise or any bill of exchange or promissory note, is brought to him after the drawing or execution thereof, on paper not duly stamped.

In effect, the proviso to Section 32(3) lays down the time limit within which the Collector of Stamps can make any endorsement on any instrument brought to him, for his opinion as to the duty chargeable thereon.

#### **INSTRUMENTS NOT DULY STAMPED – TREATMENT AND CONSEQUENCES (IMPOUNDING)**

- (a) The definition of the term “duly stamped” has already been explained. Chapter IV of the Act (consisting of Sections 35 to 48) provides for the consequences that follow where instruments are not duly stamped.

Section 33 contains a mandate on certain officials to impound an instrument which is not duly stamped. Section 33(1) provides that every person having by law or consent of parties, authority to receive evidence and every person in charge of a public office, except an officer of police before whom any instrument, chargeable in his opinion, with duty is produced or comes in the performance of his functions, shall, if it appears to him that the instrument is not duly stamped, impound the same. The object of this Section is to protect the revenue, and the Court or public officer authorised by this Section must, exercise the powers under the Section *suo moto* and the jurisdiction of the Court does not depend upon raising of an objection by the parties. For the purposes of this section, the State Government may determine what offices are public offices. The Section also provides that the instrument must be impounded, before it can be admitted in evidence. Once it is admitted in evidence, the instrument cannot be impounded at a later stage and a court, after it becomes *functus officio*, cannot rectify an earlier error.

- (b) **The word ‘produced’ has to be properly understood. It means produced in response to a summon or produced voluntarily for some judicial purpose, such as, for supporting an evidence. It does not refer to a document which accidentally or incidentally falls into a judge’s hand. The Court is not justified in impounding a document which the witness had not been called upon to produce (*Narayandas v. Nathuram*, ILR 1943 Nag. 520; AIR 1943 Nag. 97). Similarly, a Court before which a copy of a document has been produced cannot compel the party to produce the original document with a view to impounding it, having received information that is not sufficiently stamped. It is open to the party to refuse to obey the order of the Court in this respect (*Uttam Chand v. Permanand*, AIR 1942 Lah. 265).**
- (c) Where a magistrate issued a warrant with a view to discovering registers kept by the accused *containing documents not stamped in accordance with the provisions* of the Stamp Act, and in course of the search, the registers were seized and produced before the magistrate, it was held that the documents thus produced could be impounded as the word ‘comes’ is sufficiently wide to include documents produced by the search under a search warrant (*Emperor v. Balu Kuppayyan*, ILR 25 Mad. 525). This case should be confined to its facts.
- (d) An arbitrator has the consent of parties to adjudicate the issues coming before him and where the parties tender evidence, an arbitrator has a statutory duty under Section 33(1) to check whether the instrument so produced is duly stamped and if not, to impound the same.
- (e) However, this shall not compel any magistrate or judge of a Criminal Court to examine or impound (if he does not think it fit to do so) any instrument coming before him in the course of any

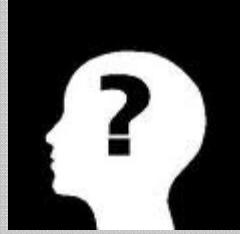
proceeding other than possession proceedings and maintenance proceedings. Also, a judge of a High Court can delegate the duty of examining and impounding any instrument to any other person appointed by the court in this behalf.

### Test your knowledge

**State whether the following statement is “True” or “False”**

Section 18 facilitates the stamping of the documents within a period of three months.

- True
- False



**Correct answer: True**

## UNSTAMPED RECEIPTS

Section 34 provides that where the instrument is an unstamped receipt produced in the course of an audit of any public account, the officer before whom the receipt is produced has a discretion either to impound or to require the receipt to be stamped. This section applies where the receipt is chargeable with a duty not exceeding 10 naya paisa. The officer concerned can, instead of impounding the receipt require a duly stamped receipt to be substituted therefor.

## INSTRUMENTS NOT DULY STAMPED INADMISSIBLE IN EVIDENCE

- (a) Section 35 stipulates that no instrument chargeable with duty shall be–
- (i) admitted in evidence *for any purpose* whatsoever by any person authorised by law (such as judges or commissioners) or by the consent of the parties (such as arbitrators) to record evidence; or
  - (ii) shall be acted upon; or
  - (iii) registered; or
  - (iv) authenticated by any such person as aforesaid or by any public officer.
- unless such instrument is duly stamped.

An insufficiently stamped instrument is not an invalid document and it can be admitted in evidence on payment of penalty.

[See *K. Narasimha Rao v. Sai Vishnu*, AIR 2006 AP 80 also at p.302]

Photocopy of an agreement not being an ‘instrument’ such copy of document which is unstamped can not be validated by payment of stamp duty and penalty. *Ashok Kalam Capital Builders v. State & Anr.*, AIR 2010 (NOC) 736 (Del).

- (b) The proviso to Section 35 provides as under:

- (i) any instrument not being an instrument chargeable with a duty not exceeding 10 naya paisa only, or a bill of exchange, or promissory note, subject to all such expectations, be admitted in evidence on payment of the duty with which the same is chargeable, or, in the case of an instrument insufficiently stamped, of the amount required to make up such duty, together with a penalty of Rs. 5/- or when ten times the amount of the proper duty or deficient portion thereof exceeds Rs. 5/-, on a sum equal to ten times such duty or portion;

- (ii) where any person from whom a stamped receipt could have been demanded has given an unstamped receipt and such receipt, if stamped, would be admissible in evidence against him, on payment of a penalty of Re. 1/- by the person tendering it;
- (iii) where a contract or agreement of any kind is affected by the correspondence consisting of two or more letters and any one of the letters bears the proper stamp, the contract or agreement shall be deemed to be duly stamped;
- (iv) nothing contained in Section 35 shall prevent the admission of any instrument in evidence in any proceeding in a criminal Court other than the proceeding under Chapter XII or Chapter XXXVI of the Code of Criminal Procedure, 1898;
- (v) also nothing contained in Section 35 shall prevent the admission of any instrument in the Court, when such instrument has been executed by or on behalf of the Government, or where it bears the certificate of the Collector as provided by Section 32 or any other provision of the Act.
- (c) The words 'shall not be admissible in evidence' used in this Section only means that the *document* shall not be made the basis of the decision or should not be relied upon to support any finding (*Sheonath Prasad v. Sorjoo Nonia*, 1943 ALJ, 189; AIR 1943 All 220 (FB)). There is no embargo upon proving the surrounding circumstances.
- (d) The words 'for any purpose' used in this Section would have their natural meaning. Where an unstamped document is admitted in proof of some collateral matter, it is certainly admitted in evidence for that purpose, which the Act prohibits. In *Ram Ratan v. Parmanand*, ILR 1946 Lah. 63, it was held that an unstamped partition deed cannot be used to corroborate the oral evidence for the purpose of determining even the factum of partition as distinct from its term. The words 'for any purpose' would in effect mean 'for each and every purpose whatsoever without any exception'.
- (e) It is immaterial whether the purpose is the main purpose or a collateral one. The words 'acted on' means that nothing can be recovered under the instrument unless it has a proper stamp. Similarly, where a suit is brought upon an instrument which is not duly stamped, the admission of the contents of the instrument made by the defendant does not avail the claimant and a decree cannot be based on such instruments. Admitting an instrument in evidence also amounts to acting upon it and an instrument which should have been stamped but is not stamped is not admissible in evidence for any purpose whatsoever.
- (f) Where an unstamped instrument is lost, the party relying on it is helpless and no payment of penalty can enable admission of secondary evidence.

### ADMISSION OF INSTRUMENTS (WHERE NOT TO BE QUESTIONED)



Section 36 provides that where an instrument has been admitted in evidence, such an admission shall not (except as provided in Section 61) be called in question at any stage of the same suit or proceeding on the ground that the instrument has not been duly stamped. Section 36 is mandatory (*Guni Ram v. Kodar*, AIR 1971 All 434, 437).

If notwithstanding any objection, the trial Court admits the document, the matter ends there and the Court cannot subsequently order the deficiency to be made and levy penalty (*Bhupathi Nath v. Basanta Kumar*, AIR 1936 Cal. 556; AIR 1933 Lah. 240).

However, it should be mentioned that Section 61 makes certain important provisions, details of which will be discussed later.

## ADMISSION OF IMPROPERLY STAMPED INSTRUMENTS

Under Section 37, opportunity is given to a party, of getting a mistake rectified when a stamp of proper amount, but of improper description has been used. Under this section, the State Government may make rules providing that, where an instrument bears a stamp of sufficient amount but of improper description, the instrument may, on payment of the duty with which the stamp is chargeable, be certified to be duly stamped, and any instrument so certified shall then be deemed to have been duly stamped as from the date of its execution.

## DEALING WITH INSTRUMENTS IMPOUNDED

- (a) Section 38 deals with instruments impounded under Section 33. A person impounding an instrument under Section 33 and receiving the same in evidence (upon payment of penalty under Section 35 or, of duty under Section 37) shall send, to the Collector of Stamps, an authenticated copy of such instrument, together with a certificate in writing, stating the amount of duty and penalty levied in respect thereof and shall send such amount to the Collector or to such person as the Collector may appoint in this behalf. In every other case, the person so impounding an instrument shall send it in original to the Collector.
- (b) Section 39 vests the Collector with certain powers to refund penalty recovered by a court on impounding a document not duly stamped when produced before it. Under Section 38, the court so impounding the instrument and realising the penalty has to forward an authenticated copy of the instrument and the amount of penalty recovered to the Collector. The Collector, on examining the instrument so received by him may, in his discretion, refund the whole penalty if it had been imposed for contravention of Section 13 or Section 14 of the Act and in any other case any portion of the penalty in excess of Rs. 5/- in cases where a copy of the instrument under Section 38(1) has been sent to him. The Collector can act *suo motu* without any application in this behalf being made by a party affected.

## COLLECTOR'S POWER TO STAMP INSTRUMENT IMPOUNDED

Section 40 deals with Collector's powers to stamp an instrument which is impounded. Under Section 40(1), the Collector when impounding any instrument under Section 33, or receiving any instrument under Section 38(2) not being an instrument chargeable with duty not exceeding 10 naya paise only or a bill of exchange or promissory note, shall adopt the following procedure:

- (i) if he is of the opinion that instrument is duly stamped or is not chargeable with duty, he shall certify by endorsement thereon that it is duly stamped, or that it is not so chargeable as the case may be;
- (ii) if he is of the opinion that such instrument, is chargeable with duty and is not duly stamped, he shall require the payment of the proper duty or the amount required to make up the same, together with a penalty of Rs. 5/-, if he thinks fit an amount not exceeding ten times the amount of the proper duty or of the deficient portion thereof, whether such amount exceeds or falls short of Rs. 5/-.

The Collector, however, has the discretion to remit the whole penalty leivable under this Section in a case where the instrument has been impounded only because it has been written in contravention of Section 13 or Section 14.

A certificate given in the situation (i) above, shall, for the purposes of the Act be conclusive evidence of the matters stated therein. Sub-section (3) of Section 40 provides that an instrument which has been sent to the Collector under Section 38(2) shall be returned to the impounding officer after the collector has dealt with the same in the manner provided above.

***Test your knowledge******Choose the correct answer***

*Who can receive the stamp duty without penalty and certify an instrument as duly stamped, as from the date of execution?*

- (a) Revenue Officer
- (b) Magistrate
- (c) Collector
- (d) None of the above

**Correct answer: (c)**

**INSTRUMENTS UNDULY STAMPED BY ACCIDENT**

Section 41 deals with cases where a person, of his own motion bring it to the Collector's notice that the instrument is not duly stamped. In such cases, if the Collector is satisfied, that the omission to pay the proper duty was due to accident, mistake or urgent necessity, he may receive the deficit amount and certify by endorsement on the instrument that the proper duty has been levied. In order to avail of the benefit of this section, the instrument must be produced before the Collector within one year of the date of its execution. Where the instrument is brought to the notice of the Collector, beyond the period of one year, Section 47 has no application and the Collector has to proceed under Section 42 read with Section 33 and 40 of the Act. Where the instrument having been brought to the notice of the Collector within the period of one year, the Collector is in doubt regarding the amount of duty chargeable, he may refer the case to the Chief Controlling Revenue Authority and proceed in accordance with the decision of such authority. However, where no such reference is made by the Collector, the Collector's decision would be final, and the Chief Controlling Revenue Authority cannot interfere with his decision.

**ENDORSEMENT OF INSTRUMENT ON WHICH DUTY HAS BEEN PAID UNDER SECTIONS 35, 40 AND 41**

Section 42 deals with cases where duty and penalty, if any, have been levied and realised by the court or any other body or by the Collector. In such cases, the authority refunding and collecting the duty and penalty must make an endorsement on the instrument as to the amount paid and the name and the residence of the person paying the same. Upon such certification, the instrument becomes admissible in evidence and may be registered and acted upon as if it had been duly stamped. The duty and penalty referred to in this Section are those covered by Sections 35, 40 or 41 as the case may be. The proviso to this Section lays down that no instrument which has been admitted in evidence upon payment of duty and a penalty under Section 35, shall be delivered to the person from whom possession of it came into the hands of the officer impounding it, before the expiration of one month from the date of such impounding or if the Collector has certified that its further detention is necessary and has not cancelled such certificate. Again, nothing contained in Section 42 shall affect the provisions of clause (3) of Section 144 of the Code of Civil Procedure, 1889 [under the present Code the corresponding provision is proviso to Order 13, Rule 9(1)].

**PROSECUTION FOR OFFENCES AGAINST STAMP LAW**

Section 43 deals with prosecutions for offences against the Stamp Law. This section provides that a levy of a penalty or payment thereof in respect of an unstamped or insufficiently stamped document (as provided for in Chapter IV) does not necessarily exempt a person from liability for prosecution for such offence. However,

the proviso to the section clarifies that no such prosecution shall be instituted in the case of any instrument in respect of which a penalty has been paid, unless it appears to the Collector that the offence was committed with the intention of evading the payment of proper duty. On receipt of copy of the instrument impounded under Section 38, the Collector can initiate criminal proceedings if he sees reasons therefor.

### RECOVERY OF DUTY OR PENALTY IN CERTAIN CASES

Section 44 deals with the circumstances in which persons paying duty or penalty may recover the same in certain cases. The duty or penalty under this Section refers to the duty or penalty paid/levied under Sections 35, 37, 40 or 41 of the Act. It also includes any duty or penalty under Section 29. The remedy is available to a person who, under the Act, was not bound to bear the expense of providing the proper stamp for such instrument. Such a person shall be entitled to recover, from the person bound to bear such expense, the amount of duty or penalty, if any, paid. For the purpose of such recovery, any certificate granted in respect of such instruments under the Act shall be conclusive evidence of the matters therein certified. Sub-section (3) of Section 44 further provides that the amounts so recoverable may, if the court thinks fit, be included in any order as to cost in any suit or proceedings to which such persons are parties and in which such instrument has been tendered in evidence. If the court does not include the amount in such order, no further proceedings for the recovery of the amount shall be maintainable.

### REFUND OF DUTY OR PENALTY IN CERTAIN CASES BY REVENUE AUTHORITY

Section 45 deals with power of the Revenue Authority to refund the penalty in excess of duty payable on instrument in certain cases. Section 39 of the Act empowers the Collector to refund a part and in some cases, the whole of the penalty paid under the provisions of Section 35. Section 45 further empowers the Chief Controlling Revenue Authority to order refunds. The object of granting such further power to the Chief Controlling Revenue Authority is evidently to set right mistakes or other omissions by the Collector to order refund in deserving cases. The Section provides that where any penalty is paid under Section 35 or Section 40, the Chief Controlling Revenue Authority may, upon application in writing made within one year from the date of payment, order, refund such penalty wholly or in part. Where in the opinion of the Chief Controlling Revenue Authority, stamp duty in excess of that which is legally chargeable has been charged and paid under Section 35 or Section 40, such authority may, upon application in writing made within three months of the order charging the same, refund the excess.

It is necessary to appreciate the differences between the powers of the Collector under Section 39 and the powers of the Controlling Revenue Authority under Section 45 at this stage. They are:

- (i) Section 39 provides for refund of penalty, whereas Section 45 confers powers to refund even duties where they have been paid in excess.
- (ii) The Collector's power to refund penalty is restricted only to two cases mentioned in Section 39(3) but the powers under Section 45 are not subject to any such limitation.
- (iii) Section 39 does not lay down any time limit for the Collector to exercise his powers to refund, but in the case of Section 45 there is a time limit.
- (iv) The power under Section 45 is to be exercised only when an application is made by a party, whereas under Section 39 it is routine function of the Collector.

The power under Section 45 is a purely discretionary one and the Chief Controlling Revenue Authority cannot be compelled to exercise his power by any further proceedings.

## NON-LIABILITY FOR LOSS OF INSTRUMENTS SENT UNDER SECTION 38

Section 46 provides that where any instrument sent to the Collector under Section 38(2) is lost, destroyed during transmission, the person sending the same, shall not be liable for such loss, destruction or damage.

However, Section 38(2) provides that when any instrument is to be sent, the person from whose possession it came into the hands of the person impounding the same may require a copy thereof to be made at his expense and authenticated by the person impounding such instruments.

## POWER TO STAMP IN CERTAIN CASES

Under Section 47 when any bill exchange or promissory note chargeable with a duty not exceeding 10 naya paise is presented for payment unstamped, the person to whom it is so presented may affix thereto the necessary adhesive stamp, and, upon cancelling the same in the manner provided in the Act, may pay the sum payable upon such bill or note and may charge the duty against the person who ought to have paid the same, or deduct it from the sum payable as aforesaid and such bill or note shall, so far as respects the duty, be deemed good and valid. However, nothing contained in this section shall relieve any person from any penalty or proceeding to which he may be liable in relation to such bill or note.

## RECOVERY OF DUTIES AND PENALTIES

Under Section 48, all duties penalties and other sums required to be paid under this Chapter may be recovered by the Collector by distress and sale of the movable property of the person or by any other process used for the recovery of the arrears of land revenue. This section provides for the mode of realisation of duty or penalty or other sums not voluntarily paid.

## ALLOWANCE AND REFUND

Section 49 deals with different circumstances in which refund would be admissible in respect of impressed stamps not used. The section applies only to impressed stamps and not adhesive stamps. Clause (a) of the section refers to cases where the stamp paper is spoiled before any document has been written thereon, or is spoiled in the course of writing and before execution. Clause (b) refers to cases where the document has been written out wholly or in part but not executed. Clause (c) refers to bills of exchange payable otherwise than on demand and promissory notes, when these have not been accepted or made use of. Clause (d) deals with refunds after execution.

Section 49 provides that subject to such rule as may be made by the State Government, as to the evidence to be required, or the enquiry to be made, the Collector may, on application made within the period prescribed in Section 50, and if he is satisfied as to the facts, make allowance for impressed stamps spoiled in the cases hereinafter mentioned, namely:

- (a) the stamp on any paper inadvertently and undesignedly spoiled, obliterated or by error in writing or any other means rendered unfit for the purpose intended before any instrument written thereon is executed by any person;
- (b) the stamp on any document which is written out wholly or in part; but which is not signed or executed by any party thereto;
- (c) in the case of bills of exchange payable otherwise than on demand or promissory notes:
  - (1) the stamp on any such bill of exchange signed by or on behalf of the drawer which has not been accepted or made use of in any manner whatever or delivered out of his hands for any purpose other than by way of tender for acceptance provided that the paper on which any such stamp is

impressed, does not bear any signature intended as or for the acceptance of any bill of exchange to be afterwards written thereon;

- (2) the stamp on any promissory note signed by or in behalf of the maker which has not been made use of in any manner whatever or delivered out of his hands;
- (3) the stamp used or intended to be used for any such bill of exchange or promissory note signed by, or on behalf of, the drawer thereof, but which from any omission or error has been spoiled or rendered useless, although the same, being a bill of exchange may have been presented for acceptance or accepted or endorsed, or being a promissory note may have been delivered to the payee: provided that another completed and duly stamped bill of exchange or promissory note is produced identical in every particular, except in the correction of such omission or error as aforesaid, with the spoiled bill, or note;
- (d) The stamp used for an instrument executed by any party thereto which—
  - (1) has been afterwards found to be absolutely void in law from the beginning;
  - (2) has been afterwards found unfit, by reason of any error or mistake therein, for purpose originally intended;
  - (3) by reason of the death of any person by whom it is necessary that it should be executed, without having executed the same, or of the refusal of any such person to execute the same, cannot be completed so as to effect the intended transaction in the form proposed;
  - (4) for want of the execution thereof by some material party, and his inability or refusal to sign the same, is in fact incomplete and insufficient for the purpose for which it was intended;
  - (5) by reason of the refusal of any person to act under the same or to advance any money intended to be thereby secured or by the refusal or non-acceptance of any office thereby granted, totally fails of the intended purpose;
  - (6) becomes useless in consequence of the transaction intended to be thereby effected being effected by some other instrument between the same parties and bearing a stamp of not less value;
  - (7) is deficient in value and the transaction intended to be thereby effected has been effected by some other instrument between the same parties and bearing a stamp of not less value;
  - (8) is inadvertently and undesignedly spoiled, and in lieu whereof another instrument made between the same parties and for the same purpose is executed and duly stamped.

Provided that, in the case of an executed instrument, no legal proceeding has been commenced in which the instrument could or would have been given or offered in evidence and that the instrument is given up to be cancelled.

### TIME LIMITS

Section 50 prescribes the time limit within which an application for relief in respect of impressed stamps spoiled, can be made; different time limits have been specified for the purpose, namely:

- (1) in the cases mentioned in clause (d)(5) of Section 49, within two months of the date of the instrument;
- (2) in the case of a stamped paper on which no instrument has been executed by any of the parties thereto, within six months after the stamp has been spoiled;

- (3) in the case of a stamped paper in which an instrument has been executed by any of the parties thereto, within six months after the date of the instrument, or if it is not dated, within six months after the execution thereof by the person by whom it was first or alone executed:

Provided that –

- (a) when the spoiled instrument has been for sufficient reasons sent out of India, the application may be made within six months after it has been received back in India.
- (b) when, from unavoidable circumstances, any instrument for which another instrument has been substituted, cannot be given up to be cancelled within the aforesaid period, the application may be made within six months after the date of execution of the substituted instrument.

## UNUSED FORMS

Section 51 of the Act enables the Chief Controlling Revenue Authority or the Collector if authorised by the Chief Controlling Revenue Authority, for such purpose to allow refunds in cases where refunds of stamps on printed forms used by bankers, incorporated companies/bodies corporate if required. Allowance may be made without limit of time, for stamped papers used for printed forms of instruments any bankers or by any incorporated company or other body corporate, if for any sufficient reasons such forms have ceased to be required by the said banker, company or body corporate: provided that the Chief Controlling Revenue Authority or the Collector, as the case may be, is satisfied that the duty in respect of such stamped papers has been duly paid.

## MISUSED STAMPS

Section 52 deals with allowance for misused stamps and applies to both impressed and adhesive stamps in the following instances:

- (a) When any person has inadvertently used, for an instrument chargeable with duty, a stamp of a description other than that prescribed for such instrument by the rules made under this Act, or a stamp of greater value than was necessary, or has inadvertently used any stamp for an instrument not chargeable with any duty; or
- (b) When any stamp used for an instrument has been inadvertently rendered useless under Section 15, owing to such instrument having been written in contravention of the provisions of Section 13.

The Collector may, on application made within six months after the date of instrument or, if it is not dated, within six months after the execution thereof by the person by whom it was first or alone executed, and upon the instrument, if chargeable with duty, being restamped with the proper duty, cancel and allow as spoiled the stamp so misused or rendered useless.

Under Section 53, in any case in which allowance is made for spoiled or misused stamps, the Collector may give in lieu thereof:

- (a) other stamps of the same description and value; or
- (b) if required and he thinks fit, stamps of any other description to the same amount in value; or
- (c) at his discretion, the same value in money, deducting ten naya paisa for each rupee or fraction of a rupee.

Section 54 of the Act enables a person to obtain refund of the value of stamps purchased by him, if he has no immediate use thereof. Under this section, when any person is possessed of a stamp or stamps which have not been spoiled or rendered unfit or useless for the purpose intended, but for which he has no

immediate use, the Collector shall repay to such person the value of such stamp or stamps in money, deducting ten naya paise for each rupee or portion of a rupee, upon such person delivering up the same to be cancelled and proving to the Collector's satisfaction

- (a) that such stamp or stamps were purchased by such person with a *bona fide* intention to use them; and
- (b) that he has paid the full price thereof; and
- (c) that they were so purchased within the period of six months next preceding the date on which they were so delivered.

Provided that, where the person is a licensed vendor of stamps, the Collector may, if he thinks fit, make the repayment of the sum actually paid by the vendor without any such deduction as aforesaid.

### ***Test your knowledge***

***State whether the following statement is “True” or “False”***

*Section 44 deals with the power of the Revenue Authority.*

- *True*
- *False*



***Correct answer: False***

## **DEBENTURES**

Section 55 is intended to relieve companies renewing debentures issued by them from the liability to pay stamp duty on both the original and the renewed debenture. As per this section, when any duly stamped debenture is renewed by the issue of a new debenture in the same terms, the Collector shall, upon application made within one month, repay to the person issuing such debenture, the value of the stamp on the original or on the new debenture whichever shall be less:

Provided that the original debenture is produced before the Collector and cancelled by him in such manner as the State Government may direct.

A debenture shall be deemed to be renewed in the same terms within the meaning of this section notwithstanding the following changes:

- (a) the issue of two or more debentures in place of one original debenture, the total amount secured being the same;
- (b) the issue of one debenture in place of two or more original debentures, the total amount secured being the same;
- (c) the substitution of the name of the holder at the time of renewal for the name of the original holder; and
- (d) the alteration of the rate of interest or the date of payment hereof.

## **REFERENCE AND REVISION**

Sections 56 to 61 deal with Reference and Revision. Section 56 provides that the powers exercisable by a Collector under Chapter IV and V and under clause (a) of the first proviso to Section 26 shall in all cases be

subject to the control of the Chief Controlling Revenue Authority. Further, if any Collector, acting under Sections 31, 40 or 41, feels doubt as to the amount of duty with which any instrument is chargeable, he may draw up a statement of the case, and refer it, with his own opinion thereon, for the decision of the Chief Controlling Revenue Authority [Section 56(2)].

Such authority shall consider the case and send a copy of its decision to the Collector, who shall proceed to assess and charge the duty (if any) in conformity with such decision.

As per Section 57(1), the Chief Controlling Revenue Authority may state any case referred to it under Section 56(2) or otherwise coming to its notice, and refer such case, with its own opinion thereon to the High Court and the same shall be decided by not less than three Judges of the High Court and the majority decision shall prevail.

According to Section 58, if the High Court is not satisfied that the statements contained in the case are sufficient to enable it to determine the questions raised thereby, the court may refer the case back to the Revenue Authority for further feed back. The High Court shall decide the questions raised and give its judgment to the Authority who shall dispose of the case as per the judgment.

As per Section 60, any subordinate Court can also refer such case to the High Court like the Revenue Authority but should be through proper channel. In Section 61(1) of the Act it is provided that a Court may take into consideration on its own motion or on application of the Collector, an order of the lower Court admitting the instrument as duly stamped or as not requiring stamp duty or on payment of duty and penalty. According to sub-section 2 of Section 61, if such Court is not in agreement with the stand of the lower Court, it may require that the instrument be produced before it and may even impound the same if necessary. While doing so, the Court shall send a copy of its order to the Collector and to the office/Court from which such instrument has been received. [Section 61(3)]

## PROSECUTION

As per Section 61(4), the Collector has got the power notwithstanding anything contained in the order of the lower court, to prosecute a person if any offence against the Stamp Act which he considers that the person has committed in respect of such an instrument. The prosecution is instituted when he is satisfied that the offence is committed with an intention of evading the proper stamp duty. The order of the lower Court as to the instrument shall be valid except for the purposes of prosecution in this respect.

## CRIMINAL OFFENCES

Sections 62 to 72 deal with penalties for offences. The provisions are as under:

- (1) As per Section 62(1), any person
  - (a) drawing, making, issuing, endorsing or transferring, or signing otherwise than as a witness, or presenting for acceptance or payment, or accepting, paying or receiving payment of or in any manner negotiating, any bill of exchange (payable otherwise than on demand) or promissory note without the same being duly stamped; or
  - (b) executing or signing otherwise than as a witness any other instrument chargeable with duty without the same being duly stamped; or
  - (c) voting or attempting to vote under any proxy not duly stamped shall, for every such offence, be punishable with fine which may extend to five hundred rupees.

Provided that, when any penalty has been paid in respect of any instrument under Sections 35, 40 or 61, the amount of such penalty shall be allowed in reduction of the fine (if any) subsequently imposed under this section in respect of the same instrument upon the person who paid such penalty. In such a case the Collector is to make an enquiry and to give an opportunity to the

accused to pay. In such cases the instrument is (i) chargeable with duty, and (ii) there is a dishonest intention not to pay the duty.

Sub-section (2) of Section 62, provides that if a share-warrant is issued without being duly stamped, the company issuing the same, and also every person who, at the time when it is issued, its managing director or secretary or other principal officer of the company, shall be punishable with fine which may extend to five hundred rupees.

- (2) Any person required by Section 12 to cancel an adhesive stamp, and failing to cancel such stamp in the manner prescribed by that section, shall be punishable with fine which may extend to one hundred rupees (Section 63). The criminal intention is necessary for an offence under this Section.
- (3) As per Section 64, any person who, with intent to defraud the Government-
  - (a) executes any instrument in which all the facts and circumstances required by Section 27 to be set forth in such instrument are not fully and truly set forth; or
  - (b) being employed or concerned in or about the preparation of any instrument, neglects or omits fully and truly to set forth therein all such facts and circumstances; or
  - (c) does any other Act calculated to deprive the Government of any duty or penalty under this Act; shall be punishable with fine which may extend to five thousand rupees.

Here also, an intention to evade payment of proper stamp duty or intention to defraud the Government of its stamp revenue is necessary.

- (4) Any person who (a) being required under Section 30 to give a receipt, refuses or neglects to give the same; or (b) with intent to defraud the Government of any duty, upon a payment of money or delivery of property exceeding twenty rupees in amount or value, gives a receipt for amount or value not exceeding twenty rupees, or separates or divides the money or property paid or delivered shall be punishable with fine which may extend to one hundred rupees (Section 65). To constitute an offence under this section, an intention to defraud the Government is necessary.
- (5) As per Section 66, any person shall be punishable with fine which may extend to Rs. 200/- if he –
  - (a) receives, or takes credit for any premium or consideration for any contract of insurance and does not, within one month after receiving or taking credit for, such premium or consideration, make out and execute a duly stamped policy of such insurance; or
  - (b) makes, executes or delivers out any policy which is not duly stamped or pays or allows in account, or agrees to pay or to allow in account, any money upon, or in respect of, any such policy.
- (6) As per Section 67, if any person drawing or executing a bill of exchange (payable otherwise than on demand) or a policy of marine insurance purporting to be drawn or executed in a set of two or more, and not at the same time drawing or executing on paper duly stamped the whole number of bills or policies of which such bill or policy purports the set to consist, shall be punishable with fine which may extend to one thousand rupees.
- (7) Any person who, (a) with intent to defraud the Government, of duty, draws, makes or issues any bill of exchange or promissory note bearing a date subsequent to that on which such bill or note is actually drawn or made; or (b) knowing that such bill or note has been so post-dated, endorses, transfers, presents for acceptance or payment, or accepts, pays or receives payment of, such bill or note; or in any manner negotiates the same; (c) with the like intent, practices or is concerned in any act, contrivance or device not specially provided for by this Act or any other law for the time being in force; shall be punishable with fine which may extend to one thousand rupees. Intention to defraud is an essential ingredient for offence under Section 68.

(8) If any person appointed to sell stamps who disobeys any rule made under Section 74, and any person not so appointed who sells or offers for sale any stamp [other than a (ten naya paise or five naya paise) adhesive stamp] shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to five hundred rupees, or with both (section 69). Before instituting criminal proceedings under this section against any person, sanction of the Collector must be obtained. Otherwise, the proceedings will be vitiated. A criminal court having jurisdiction to try offences under Cr. P.C. can try such offences.

### **TAKING COGNIZANCE**

- (a) No prosecution in respect of any offence punishable under this Act or any Act hereby repealed, shall be instituted without the sanction of the Collector or such other officer as the State Government generally or the Collector specially, authorises in that behalf.
- (b) The Chief Controlling Revenue Authority, or any officer generally or specially authorised by it in this behalf, may stay any such prosecution or compound any such offence.
- (c) The amount of any such composition shall be recoverable in the manner provided by Section 48.

A Magistrate other than a Presidency Magistrate or a Magistrate whose powers are not less than those of a Magistrate of the second class, shall try any offence under this Act (Section 71).

Every such offence committed in respect of any instrument may be tried in any district or presidency town in which instrument is found as well as in any district or presidency town in which such offence might be tried under the Code of Criminal Procedure for the time being in force (Section 72).

### **MISCELLANEOUS PROVISIONS**

Chapter VIII, containing Sections 73 to 78 deals with supplemental provisions regarding inspection of relevant registers, books, records, etc; to enter the premises for that purpose, powers of Government to frame rules for the sale and supply of stamps and to make rules generally to carry out the provisions of the Act.

Section 77A provides that all stamps in denominations of annas four or multiples thereof shall be deemed to be stamps of the value of 25 naya paise or (as the case may be), multiples thereof and shall accordingly be valid for all the purposes of the Act. From this it can be inferred that whatever the stamp duty is mentioned to be annas in the first Schedule; the instrument concerned has to be treated as leviable with duty of 25 naya paise or in multiples thereof as the case may be.

### **SCHEDULE**

The Schedule to the Stamp Act prescribes the rates of stamp duties on instruments. Articles 13, 27, 37, 47, 49, 53 and 62(a) of the Schedule relate to instruments, the rates of duties on which are prescribed by the Central Legislature and have been subject to legislative amendments by that Legislature (See Entry 91 of List I). The other articles relate to instruments in respect of which the Central Legislature has lost its power to regulate rates of duties (except for Union Territories) since the passing of the Government of India Act, 1935. With respect to these instruments, the rates mentioned are fixed by the State Legislatures (See Entry 63 of List II).

### **E-STAMPING**

E-Stamping is a computer based application and a secured way of paying Non-Judicial stamp duty to the Government. The benefits of e-Stamping are e-Stamp Certificate can be generated within minutes; e-Stamp Certificate generated is tamper proof; Easy accessibility and faster processing; Security; Cost savings and User friendly.

## LESSON ROUND-UP

- The Indian Stamp Act, 1899 is the law relating to stamps which consolidates and amends the law relating to stamp duty. It is a fiscal legislation envisaging levy of stamp duty on certain instruments.
- Entry 91 of the Union List, gives power to Union Legislature to levy stamp duty with regard to certain instruments (mostly of a commercial character). They are bill of exchange, cheques, promissory notes, bill of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies and receipt. Likewise, entry 63 of the State List confers on the States power to prescribe the rates of stamp duties on other instruments.
- Instrument includes every document by which any right or liability, is, or purported to be created, transferred, limited, extended, extinguished or recorded. Any instrument mentioned in Schedule I to Indian Stamp Act is chargeable to duty as prescribed in the schedule.
- In case of sale, mortgage or settlement, if there are several instruments for one transaction, stamp duty is payable only on one instrument. On other instruments, nominal stamp duty of Re. 1 is payable. If one instrument relates to several distinct matters, stamp duty payable is aggregate amount of stamp duties payable on separate instruments.
- Government can reduce or remit whole or part of duties payable. Such reduction or remission can be in respect of whole or part of territories and also can be for particular class of persons. Government can also compound or consolidate duties in case of issue of shares or debentures by companies.
- The payment of stamp duty can be made by adhesive stamps or impressed stamps. Instrument executed in India must be stamped before or at the time of execution. Instrument executed out of India can be stamped within three months after it is first received in India. In some cases, stamp duty is payable on ad valorem basis, i.e. on the basis of value of property, etc. In such cases, value is decided on prescribed basis.
- An instrument not 'duly stamped' cannot be accepted as evidence by civil court, an arbitrator or any other authority authorized to receive evidence. However, the document can be accepted as evidence in criminal court. Duly stamped means that the instrument bears an adhesive or impressed stamp not less than proper amount and that such stamp has been affixed or used in accordance with law in force in India.
- If non-payment or short payment of stamp duty is by accident, mistake or urgent necessity, the person can himself produce the document to Collector within one year. In such case, Collector may receive the amount and endorse the document that proper duty has been paid.
- If the company issues securities to one or more depositories, it will have to pay stamp duty on total amount of security issued by it and such securities need not be stamped. If an investor opts out of depository scheme, the securities surrendered to Depository will be issued to him in form of a certificate. Such share certificate should be stamped as if a 'duplicate certificate' has been issued. If securities are purchased or sold under depository scheme, no stamp duty is payable.
- A levy of a penalty or payment in respect of an unstamped or insufficiently stamped document does not necessarily exempt a person from liability for prosecution for such offence. Revenue Authority has been authorized to refund the penalty in excess of duty payable on instrument in certain cases.
- The Collector has got the power notwithstanding anything contained in the order of the lower court, to prosecute a person if any offence against the Stamp Act which he considers that the person has committed in respect of such an instrument. The prosecution is instituted when he is satisfied that the offence is committed with an intention of evading the proper stamp duty. The order of the lower court as to the instrument shall be valid except for the purposes of prosecution in this respect.
- Provisions have been incorporated in the Act to relieve companies renewing debentures issued by them from the liability to pay stamp duty on both the original and the renewed debenture.

## **SELF-TEST QUESTIONS**

1. Define the expression “bond”.
  2. D executes an agreement in favour of C, (with witnesses) by which he promises to repay a loan taken by him from C. Discuss whether this is an agreement, a promissory note or a bond.
  3. Is an agreement for the sale of goods “conveyance”, for the purposes of the Stamp Act? Discuss.
  4. A document creates a lease of property X and also grants a gift of property Y. How is the stamp duty to be calculated, on this document?
  5. Can Parliament increase or, decrease, the stamp duty on an agreement?

# Lesson 8

## LAW RELATING TO CONTRACT

### LESSON OUTLINE

- Meaning and Nature of contract
- Agreement
- Essential elements of a valid contract
- Flaws in Contract
- Agreement that restrained of Trade
- Wagering Agreement
- Void Agreement
- Quantum Meruit
- Restitution
- Contingent Contract
- Quasi Contract
- Contract of Indemnity Guarantee
- Remedies for Breach
- Contract of Bailment and Pledge
- Law of Agency
- Del Credere Agent
- Termination of Agency
- When termination takes effect
- Joint Venture Agreements
- E-Contract

### LEARNING OBJECTIVES

A contract is an agreement enforceable at law, made between two or more persons, by which rights are acquired by one or more to acts or forbearances on the part of the other or others. A contract is an agreement creating and defining obligations between the parties.

The Indian Contract Act, 1872 regulates all the transactions of a company. It lays down the general principles relating to the formation and enforceability of contracts; rules governing the provisions of an agreement and offer; the various types of contracts including those of indemnity and guarantee, bailment and pledge and agency. It also contains provisions pertaining to breach of a contract.

The Law of Contract constitutes the most important branch of Mercantile or Commercial Law. It affects everybody, more so, trade, commerce and industry. It may be said that the contract is the foundation of the civilized world. Therefore, it is essential for the students to be familiar with the law relating to Contract.

“Every agreement and promise enforceable at law is a contract”.

—*Sir Fredrick Pollock*

“A contract is an agreement creating and defining obligations between the parties “.

—*Salmond*

## MEANING AND NATURE OF CONTRACT

The law relating to contract is governed by the Indian Contract Act, 1872. The Act came into force on the first day of September, 1872. The preamble to the Act says that it is an Act "to define and amend certain parts of the law relating to contract". It extends to the whole of India except the State of Jammu and Kashmir. The Act is by no means exhaustive on the law of contract. It does not deal with all the branches of the law of contract. Thus, contracts relating to partnership, sale of goods, negotiable instruments, insurance etc. are dealt with by separate Acts.

The Indian Contract Act mostly deals with the general principles and rules governing contracts. The Act is divisible into two parts. The first part (Section 1-75) deals with the general principles of the law of contract, and therefore applies to all contracts irrespective of their nature. The second part (Sections 124-238) deals with certain special kinds of contracts, namely contracts of Indemnity and Guarantee, Bailment, Pledge, and Agency.

The Indian Contract Act has defined contract in Section 2(h) as "an agreement enforceable by law".

These definitions indicate that a contract essentially consists of two distinct parts. First, there must be an agreement. Secondly, such an agreement must be enforceable by law. To be enforceable, an agreement must be coupled with an obligation.

A contract therefore, is a combination of the two elements: (1) an agreement and (2) an obligation.

### Agreement

An agreement gives birth to a contract. As per Section 2(e) of the Indian Contract Act "every promise and every set of promises, forming the consideration for each other, is an agreement. It is evident from the definition given above that an agreement is based on a promise. What is a promise? According to Section 2(b) of the Indian Contract Act "when the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise. An agreement, therefore, comes into existence when one party makes a proposal or offer to the other party and that other party signifies his assent thereto. In nutshell, an agreement is the sum total of offer and acceptance."

An analysis of the definition given above reveals the following characteristics of an agreement:

- Plurality of persons:* There must be two or more persons to make an agreement because one person cannot enter into an agreement with himself.
- Consensus ad idem:* The meeting of the minds is called *consensus-ad-idem*. It means both the parties to an agreement must agree about the subject matter of the agreement in the same sense and at the same time.

### Obligation

An obligation is the legal duty to do or abstain from doing what one has promised to do or abstain from doing. A contractual obligation arises from a bargain between the parties to the agreement who are called the promisor and the promisee. Section 2(b) says that when the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted; and a proposal when accepted becomes a promise. In broad sense, therefore, a contract is an exchange of promises by two or more persons, resulting in an obligation to do or abstain from doing a particular act, where such obligation is recognised and enforced by law.

## Rights and Obligations

Where parties have made a binding contract, they have created rights and obligations between themselves. The contractual rights and obligations are correlative, e.g., A agrees with B to sell his car for Rs. 10,000 to him. In this example, the following rights and obligations have been created:

- (i) A is under an obligation to deliver the car to B.  
B has a corresponding right to receive the car.
- (ii) B is under an obligation to pay Rs. 10,00,000 to A.  
A has a correlative right to receive Rs. 10,00,000.

## Agreements which are not Contracts

Agreements in which the idea of bargain is absent and there is no intention to create legal relations are not contracts. These are:

- (a) *Agreements relating to social matters*: An agreement between two persons to go together to the cinema, or for a walk, does not create a legal obligation on their part to abide by it. Similarly, if I promise to buy you a dinner and break that promise, I do not expect to be liable to legal penalties. There cannot be any offer and acceptance to hospitality.
- (b) *Domestic arrangements between husband and wife*: In *Balfour v. Balfour* (1919) 2 KB 571, a husband working in Ceylon, had agreed in writing to pay a housekeeping allowance to his wife living in England. On receiving information that she was unfaithful to him, he stopped the allowance: Held, he was entitled to do so. This was a mere domestic arrangement with no intention to create legally binding relations. Therefore, there was no contract.

Three consequences follow from the above discussion.

- (i) To constitute a contract, the parties must intend to create legal relationship.
- (ii) The law of contract is the law of those agreements which create obligations, and those obligations which have their source in agreement.
- (iii) Agreement is the genus of which contract is the specie and, therefore, all contracts are agreements but all agreements are not contracts.

## ESSENTIAL ELEMENTS OF A VALID CONTRACT

Section 10 of the Indian Contract Act, 1872 provides that “all agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void”.

The essential elements of a valid contract are:

- (i) An offer or proposal by one party and acceptance of that offer by another party resulting in an *agreement—consensus-ad-idem*.
- (ii) An intention to create legal relations or an intent to have legal consequences.
- (iii) The agreement is supported by a lawful consideration.
- (iv) The parties to the contract are legally capable of contracting.
- (v) Genuine consent between the parties.

- (vi) The object and consideration of the contract is legal and is not opposed to public policy.
- (vii) The terms of the contract are certain.
- (viii) The agreement is capable of being performed i.e., it is not impossible of being performed.

Therefore, to form a valid contract there must be (1) an agreement, (2) based on the genuine consent of the parties, (3) supported by a lawful consideration, (4) made for a lawful object, and (iv) between the competent parties.

### **(a) Offer or Proposal and Acceptance**

One of the early steps in the formation of a contract lies in arriving at an agreement between the contracting parties by means of an offer and acceptance. Thus, when one party (the offeror) makes a definite proposal to another party (the offeree) and the offeree accepts it in its entirety and without any qualification, there is a meeting of the minds of the parties and a contract comes into being, assuming that all other elements are also present.

#### **What is an Offer or a Proposal?**

A proposal is also termed as an offer. The word 'proposal' is synonymous with the English word "offer". An offer is a proposal by one person, whereby he expresses his willingness to enter into a contractual obligation in return for a promise, act or forbearance. Section 2(a) of the Indian Contract Act defines proposal or offer as "when one person signifies to another his willingness to do or abstain from doing anything with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal". The person making the proposal or offer is called the *proposer or offeror* and the person to whom the proposal is made is called the *offeree*.

#### **Rules Governing Offers**

A valid offer must comply with the following rules:

- (a) An offer must be clear, definite, complete and final. It must not be vague. For example, a promise to pay an increased price for a horse if it proves lucky to promisor, is too vague and is not binding.
- (b) An offer must be communicated to the offeree. An offer becomes effective only when it has been communicated to the offeree so as to give him an opportunity to accept or reject the same.
- (c) The communication of an offer may be made by express words-oral or written-or it may be implied by conduct. A offers his car to B for Rs. 10,000. It is an express offer. A bus plying on a definite route goes along the street. This is an implied offer on the part of the owners of the bus to carry passengers at the scheduled fares for the various stages.
- (d) The communication of the offer may be general or specific. Where an offer is made to a specific person it is called specific offer and it can be accepted only by that person. But when an offer is addressed to an uncertain body of individuals i.e. the world at large, it is a general offer and can be accepted by any member of the general public by fulfilling the condition laid down in the offer. The leading case on the subject is *Carlill v. Carbolic Smoke Ball Co.* The company offered by advertisement, a reward of # 100 to anyone who contacted influenza after using their smoke ball in the specified manner. Mrs. Carlill did use smoke ball in the specified manner, but was attacked by influenza. She claimed the reward and it was held that she could recover the reward as general offer can be accepted by anybody. Since this offer is of a continuing nature, more than one person can accept it and can even claim the reward. But if the offer of reward is for seeking some information or seeking the restoration of missing thing, then the offer can be accepted by one

individual who does it first of all. The condition is that the claimant must have prior knowledge of the reward before doing that act or providing that information.

*Example:* A advertise in the newspapers that he will pay rupees one thousand to anyone who restores to him his lost son. B without knowing of this reward finds A's lost son and restore him to A. In this case since B did not know of the reward, he cannot claim it from A even though he finds A's lost son and restores him to A.

In India also, in the case of *Harbhajan Lal v. Harcharan Lal* (AIR 1925 All. 539), the same rule was applied. In this case, a young boy ran away from his fathers home. The father issued a pamphlet offering a reward of Rs. 500 to anybody who would bring the boy home. The plaintiff saw the boy at a railway station and sent a telegram to the boys father. It was held that the handbill was an offer open to the world at large and was capable to acceptance by any person who fulfilled the conditions contained in the offer. The plaintiff substantially performed the conditions and was entitled to the reward offered.

### An Offer must be Distinguished from

(a) *An invitation to treat or an invitation to make an offer:* e.g., an auctioneers request for bids (which are offered by the bidders), the display of goods in a shop window with prices marked upon them, or the display of priced goods in a self- service store or a shopkeepers catalogue of prices are invitations to an offer.

(b) *A mere statement of intention:* e.g., an announcement of a coming auction sale. Thus, a person who attended the advertised place of auction could not sue for breach of contract if the auction was cancelled (*Harris v. Nickerson* (1873) L.R. 8 QB 286).

(c) *A mere communication of information in the course of negotiation:* e.g., a statement of the price at which one is prepared to consider negotiating the sale of piece of land (*Harvey v. Facey* (1893) A.C. 552).

An offer that has been communicated properly continues as such until it lapses, or until it is revoked by the offeror, or rejected or accepted by the offeree.

### Lapse of Offer

Section 6 deals with various modes of lapse of an offer. It states that an offer lapses if—

- (a) it is not accepted within the specified time (if any) or after a reasonable time, if none is specified.
- (b) it is not accepted in the mode prescribed or if no mode is prescribed in some usual and reasonable manner, e.g., by sending a letter by mail when early reply was requested;
- (c) the offeree rejects it by distinct refusal to accept it;
- (d) either the offeror or the offeree dies before acceptance;
- (e) the acceptor fails to fulfill a condition precedent to an acceptance.
- (f) the offeree makes a counter offer, it amounts to rejection of the offer and an offer by the offeree may be accepted or rejected by the offeror.

### Revocation of Offer by the Offeror

An offer may be revoked by the offeror at any time before acceptance.

Like any offer, revocation must be communicated to the offeree, as it does not take effect until it is actually communicated to the offeree. Before its actual communication, the offeree, may accept the offer and create a binding contract. The revocation must reach the offeree before he sends out the acceptance.

An offer to keep open for a specified time (option) is not binding unless it is supported by consideration.

### Acceptance

A contract emerges from the acceptance of an offer. Acceptance is the act of assenting by the offeree to an offer. Under Section 2(b) of the Contract Act when a person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted becomes a promise..

### Rules Governing Acceptance

- (a) Acceptance may be express i.e. by words spoken or written or implied from the conduct of the parties.
- (b) If a particular method of acceptance is prescribed, the offer must be accepted in the prescribed manner.
- (c) Acceptance must be unqualified and absolute and must correspond with all the terms of the offer.
- (d) A counter offer or conditional acceptance operates as a rejection of the offer and causes it to lapse, e.g., where a horse is offered for Rs. 1,000 and the offeree counter-offers Rs. 990, the offer lapses by rejection.
- (e) Acceptance must be communicated to the offeror, for acceptance is complete the moment it is communicated. Where the offeree merely intended to accept but does not communicate his intention to the offeror, there is no contract. Mere mental acceptance is not enough.
- (f) Mere silence on the part of the offeree does not amount to acceptance.

Ordinarily, the offeror cannot frame his offer in such a way as to make the silence or inaction of the offeree as an acceptance. In other words, the offeror can prescribe the mode of acceptance but not the mode of rejection.

- (g) If the offer is one which is to be accepted by being acted upon, no communication of acceptance to the offeror is necessary, unless communication is stipulated for in the offer itself.

Thus, if a reward is offered for finding a lost dog, the offer is accepted by finding the dog after reading about the offer, and it is unnecessary before beginning to search for the dog to give notice of acceptance to the offeror.

- (h) Acceptance must be given within a reasonable time and before the offer lapses or is revoked. An offer becomes irrevocable by acceptance.

An acceptance never precedes an offer. There can be no acceptance of an offer which is not communicated. Similarly, performance of conditions of an offer without the knowledge of the specific offer, is no acceptance. Thus in *Lalman Shukla v. Gauri Dutt* (1913), where a servant brought the boy without knowing of the reward, he was held not entitled to reward because he did not know about the offer.

### Standing Offers

Where a person offers to another to supply specific goods, up to a stated quantity or in any quantity which may be required, at a certain rate, during a fixed period, he makes a standing offer. Thus, a tender to supply goods as and when required, amounts to a standing offer.

A standing offer or a tender is of the nature of a continuing offer. An acceptance of such an offer merely amounts to an intimation that the offer will be considered to remain open during the period specified and that it will be accepted from time to time by placing order for specified quantities. Each successive order given,

while the offer remains in force, is an acceptance of the standing offer as to the quantity ordered, and creates a separate contract. It does not bind either party unless and until such orders are given.

Where P tendered to supply goods to L upto a certain amount and over a certain period, L's order did not come up to the amount expected and P sued for breach of contract *Held*: Each order made was a separate contract and P was bound to fulfill orders made, but there was no obligation on L to make any order to all (*Percival Ltd. v. L.C.C.* (1918)).

### Tickets

Tickets purchased for entrance into places of amusement, or tickets issued by railways or bus companies, clock-room tickets, and many other contracts set out in printed documents contain numerous terms, of many of which the party receiving the ticket or document is ignorant. If a passenger on a railway train receives a ticket on the face of which is printed "this ticket is issued subject to the notices, regulations and conditions contained in the current time-tables of the railway", the regulations and conditions referred to are deemed to be communicated to him and he is bound by them whether or not he has read them. He is bound even if he is illiterate and unable to read them. But it is important that the notice of the conditions is contemporaneous with the making of the contract and not after the contract has been made.

### Contracts by Post

Contracts by post are subject to the same rules as others, but because of their importance, these are stated below separately:

- An offer by post may be accepted by post, unless the offeror indicates anything to the contrary.
- An offer is made only when it actually reaches the offeree and not before, i.e., when the letter containing the offer is delivered to the offeree.
- An acceptance is made as far as the offeror is concerned, as soon as the letter containing the acceptance is posted, to offerors correct address; it binds the offeror, but not the acceptor.

An acceptance binds the acceptor only when the letter containing the acceptance reaches the offeror. The result is that the acceptor can revoke his acceptance before it reaches the offeror.

- An offer may be revoked before the letter containing the acceptance is posted. An acceptance can be revoked before it reaches the offeror.

### Contracts over the Telephone

Contracts over the telephone are regarded the same in principle as those negotiated by the parties in the actual presence of each other. In both cases an oral offer is made and an oral acceptance is expected. It is important that the acceptance must be audible, heard and understood by the offeror. If during the conversation the telephone lines go "dead" and the offeror does not hear the offerees word of acceptance, there is no contract at the moment. If the whole conversation is repeated and the offeror hears and understands the words of acceptance, the contract is complete (*Kanhaiyalal v. Dineshwarchandra* (1959) AIR, M.P. 234).

#### (b) Intention to Create Legal Relations

The second essential element of a valid contract is that there must be an intention among the parties that the agreement should be attached by legal consequences and create legal obligations. If there is no such intention on the part of the parties, there is no contract between them. Agreements of a social or domestic nature do not contemplate legal relationship. As such they are not contracts.

A proposal or an offer is made with a view to obtain the assent to the other party and when that other party expresses his willingness to the act or abstinence proposed, he accepts the offer and a contract is made between the two. But both offer and acceptance must be made with the intention of creating legal relations between the parties. The test of intention is objective. The Courts seek to give effect to the presumed intention of the parties. Where necessary, the Court would look into the conduct of the parties, for much can be inferred from the conduct. The Court is not concerned with the mental intention of the parties, but rather with what a reasonable man would say, was the intention of the parties, having regard to all the circumstances of the case.

For example, if two persons agree to assist each other by rendering advice, in the pursuit of virtue, science or art, it cannot be regarded as a contract. In commercial and business agreements, the presumption is usually that the parties intended to create legal relations. But this presumption is rebuttable which means that it must be shown that the parties did not intend to be legally bound.

### (c) Consideration

#### Need for Consideration

Consideration is one of the essential elements of a valid contract. The requirement of consideration stems from the policy of extending the arm of the law to the enforcement of mutual promises of parties. A mere promise is not enforceable at law. For example, if A promises to make a gift of Rs. 500 to B, and subsequently changes his mind, B cannot succeed against A for breach of promise, as B has not given anything in return. It is only when a promise is made for something in return from the promisee, that such promise can be enforced by law against the promisor. This something in return is the consideration for the promise.

#### Definition of Consideration

Sir Fredrick Pollock has defined consideration "as an act or forbearance of one party, or the promise thereof is the price for which the promise of the other is bought".

It is "some right, interest, profit, or benefit accruing to one party or some forbearance, detriment, loss or responsibility, given, suffered or undertaken by the other" (*Currie v. Misa* (1875) L.R. 10 Ex. 153).

Section 2(d) of the Indian Contract Act, 1872 defines consideration thus: "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".

The fundamental principle that consideration is essential in every contract, is laid down by both the definitions but there are some important points of difference in respect of the nature and extent of consideration and parties to it under the two systems of law:

- (a) *Consideration at the desire of the promisor:* Section 2(d) of the Act begins with the statement that consideration must move at the desire or request of the promisor. This means that whatever is done must have been done at the desire of the promisor and not voluntarily or not at the desire of a third party. If A rushes to B's help whose house is on fire, there is no consideration but a voluntary act. But if A goes to B's help at B's request, there is good consideration as B did not wish to do the act gratuitously.
- (b) *Consideration may move from the promisee or any other person:* In English law, consideration must move from the promisee, so that a stranger to the consideration cannot sue on the contract. A

person seeking to enforce a simple contract must prove in court that he himself has given the consideration in return for the promise he is seeking to enforce.

In Indian law, however, consideration may move from the promisee or any other person, so that a stranger to the consideration may maintain a suit. In *Chinnaya v. Ramaya*, (1882) 4 Mad. 137, a lady by a deed of gift made over certain property to her daughter directing her to pay an annuity to the donor's brother as had been done by the donor herself before she gifted the property. On the same day, her daughter executed in writing in favour of the donor's brother agreeing to pay the annuity. Afterwards the donee (the daughter) declined to fulfil her promise to pay her uncle saying that no consideration had moved from him. The Court, however, held that the uncle could sue even though no part of the consideration received by his niece moved from him. The consideration from her mother was sufficient consideration.

### Privity of Contract

A stranger to a contract cannot sue both under the English and Indian law for want of privity of contract. The following illustration explains this point.

In *Dunlop Pneumatic Tyre Co. v. Selfridge Ltd.* (1915) A.C. 847, D supplied tyres to a wholesaler X, on condition that any retailer to whom X re-supplied the tyres should promise X, not to sell them to the public below D's list price. X supplied tyres to S upon this condition, but nevertheless S sold the tyres below the list price. Held: There was a contract between D and X and a contract between X and S. Therefore, D could not obtain damages from S, as D had not given any consideration for S's promise to X nor was he party to the contract between D and X.

Thus, a person who is not a party to a contract cannot sue upon it even though the contract is for his benefit. A, who is indebted to B, sells his property to C, and C the purchaser of the property, promises to pay off the debt to B. In case C fails to pay B, B has no right to sue C for there is no privity of contract between B and C.

The leading English case on the point is *Tweddle v. Atkinson* (1861) 1B and Section 393. In this case, the father of a boy and the father of a girl who was to be married to the boy, agreed that each of them shall pay a sum of money to the boy who was to take up the new responsibilities of married life. After the demise of both the contracting parties, the boy (the husband) sued the executors of his father-in-law upon the agreement between his father-in-law and his father. Held: the suit was not maintainable as the boy was not a party to the contract.

*Exception to the doctrine of privity of contract:* Both the Indian law and the English law recognize certain exceptions to the rule that a stranger to a contract cannot sue on the contract. In the following cases, a person who is not a party to a contract can enforce the contract:

- (i) A beneficiary under an agreement to create a trust can sue upon the agreement, though not a party to it, for the enforcement of the trust so as to get the trust executed for his benefit. In *Khawaja Muhammad v. Hussaini Begum*, (1910) 32 All. 410, it was held that where a Mohammedan lady sued her father-in-law to recover arrears of allowance payable to her by him under an agreement between him and her own father in consideration of her marriage, she could enforce the promise in her favour insofar as she was a beneficiary under the agreement to make a settlement in her favour, and she was claiming as beneficiary under such settlement.
- (ii) An assignee under an assignment made by the parties, or by the operation of law (e.g. in case of death or insolvency), can sue upon the contract for the enforcement of his rights, title and interest. But a mere nominee (i.e., the person for whose benefit another has insured his own life) cannot sue on the policy because the nominee is not an assignee.

- (iii) In cases of family arrangements or settlements between male members of a Hindu family which provide for the maintenance or expenses for marriages of female members, the latter though not parties to the contract, possess an actual beneficial right which place them in the position of beneficiaries under the contract, and can therefore, sue.
- (iv) In case of acknowledgement of liability, e.g., where A receives money from B for paying to C, and admits to C the receipt of that amount, then A constitutes himself as the agent of C.
- (v) Whenever the promisor is by his own conduct estopped from denying his liability to perform the promise, the person who is not a party to the contract can sue upon it to make the promisor liable.
- (vi) In cases where a person makes a promise to an individual for the benefit of third party and creates a charge on certain immovable property for the purpose, the third party can enforce the promise though, he is stranger to the contract.

### Kinds of Consideration

Consideration may be:

- (a) *Executory or future* which means that it makes the form of promise to be performed in the future, e.g., an engagement to marry someone; or
- (b) *Executed or present* in which it is an act or forbearance made or suffered for a promise. In other words, the act constituting consideration is wholly or completely performed, e.g., if A pays today Rs. 100 to a shopkeeper for goods which are promised to be supplied the next day, A has executed his consideration but the shopkeeper is giving executory consideration—a promise to be executed the following day. If the price is paid by the buyer and the goods are delivered by the seller at the same time, consideration is executed by both the parties.
- (c) Past which means a past act or forbearance, that is to say, an act constituting consideration which took place and is complete (wholly executed) before the promise is made.

According to English law, a consideration may be executory or executed but never past. The English law is that past consideration is no consideration. *The Indian law recognizes all the above three kinds of consideration.*

### Rules Governing Consideration

- (a) Every simple contact must be supported by valuable consideration otherwise it is formally void subject to some exceptions.
- (b) Consideration may be an act of abstinence or promise.
- (c) There must be mutuality i.e., each party must do or agree to do something. A gratuitous promise as in the case of subscription for charity, is not enforceable. For example, where A promises to subscribe Rs. 5,000 for the repair of a temple, and then refuses to pay, no action can be taken against him.
- (d) Consideration must be real, and not vague, indefinite, or illusory, e.g., a son's promise to "stop being a nuisance" to his father, being vague, is no consideration.
- (e) Although consideration must have some value, it need not be adequate i.e., a full return for the promise. Section 25 (Exp. II) clearly provides that "an agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate". It is upon the parties to fix their own prices. For example, where A voluntarily agreed to sell his motor car for Rs. 500 to B, it became a valid contract despite the inadequacy of the consideration.

- (f) Consideration must be lawful, e.g., it must not be some illegal act such as paying someone to commit a crime. If the consideration is unlawful, the agreement is void.
- (g) Consideration must be something more than the promisee is already bound to do for the promisor. Thus, an agreement to perform an existing obligation made with the person to whom the obligation is already owed, is not made for consideration. For example, if a seaman deserts his ship so breaking his contract of service and is induced to return to his duty by the promise for extra wages, he cannot later sue for the extra wages since he has only done what he had already contracted for: *Stilk v. Myrick* (1809).

### When Consideration not Necessary

The general rule is that an agreement made without consideration is void. But Section 25 of the Indian Contract Act lays down certain exceptions which make a promise without consideration valid and binding. Thus, an agreement without consideration is valid:

1. If it is expressed in writing and registered and is made out of natural love and affection between parties standing in a near relation to each other; or
2. If it is made to compensate a person who has already done something voluntarily for the promisor, or done something which the promisor was legally compellable to do; or
3. If it is a promise in writing and signed by the person to be charged therewith, or by his agent, to pay a debt barred by the law of limitation.
4. Besides, according to Section 185 of the Indian Contract Act, consideration is not required to create an agency.
5. In the case of gift actually made, no consideration is necessary. There need not be nearness of relation and even if it is, there need not be any natural love and affection between them.

The requirements in the above exceptions are noteworthy. The first one requires written and registered promise. The second may be oral or in writing and the third must be in writing.

### Illustrations

A, for natural love and affection, promises to give his son B Rs. 10,000. A put his promise to B into writing and registered it. This is a contract.

A registered agreement between a husband and his wife to pay his earnings to her is a valid contract, as it is in writing, is registered, is between parties standing in near relation, and is for love and affection (*Poonoo Bibi v. Fyaz Buksh*, (1874) 15 Bom L.R. 57).

But where a husband by a registered document, after referring to quarrels and disagreement between himself and his wife, promised to pay his wife a sum of money for her maintenance and separate residence, it was held that the promise was unenforceable, as it was not made for love and affection (*Rajlucky Deb v. Bhootnath* (1900) 4 C.W.N. 488).

### Whether Gratuitous Promise can be Enforced

A gratuitous promise to subscribe to a charitable cause cannot be enforced, but if the promisee is put to some detriment as a result of his acting on the faith of the promise and the promisor knew the purpose and also knew that on the faith of the subscription an obligation might be incurred, the promisor would be bound by promise (*Kedar Nath v. Gorie Mohan* 64).

It may be noted that it is not necessary that the promisor should benefit by the consideration, it is sufficient if

the promisee does some act from which a third person is benefited and he would not have done that act but for the promise of the promisor.

For example, Y requests X for loan, who agrees to give loan to Y if S gives guarantee of repayment of the loan. S gives such a guarantee of repayment by Y. Thereupon X gives loan to Y. Here S will be promisor and X the promisee, but from X's action, benefit is derived by Y and not by S. X would not have given the loan to Y had S not given the guarantee of repayment of loan. Thus, the benefit conferred on Y by X at the request of S is a sufficient consideration on the part of X as against the promise of S to repay the loan. Alternatively, it may be said that the detriment which X suffered by giving loan to Y at the request of S is sufficient consideration on the part of X in respect of the promise of S to repay the loan.

Consideration therefore, is some detriment to the promisee or some benefit to the promisor. Detriment to one person and benefit to the other are the same things looked from two angles. Ordinarily a promisor is not bound by his promise, unless some consideration is offered by the promisee.

### **Terms Must be Certain**

It follows from what has been explained in relation to offer, acceptance and consideration that to be binding, an agreement must result in a contract. That is to say, the parties must agree on the terms of their contract. They must make their intentions clear in their contract. The Court will not enforce a contract the terms of which are uncertain. Thus, an agreement to agree in the future (*a contract to make a contract*) will not constitute a binding contract e.g., a promise to pay an actress a salary to be "*mutually agreed between us*" is not a contract since the salary is not yet agreed: *Loftus v. Roberts* (1902).

Similarly, where the terms of a final agreement are too vague, the contract will fail for uncertainty. Hence, the terms must be definite or capable of being made definite without further agreement of the parties.

The legal maxim, therefore, is "*a contract to contract is not a contract*". If you agree "subject to contract" or "subject to agreement", the contract does not come into existence, for there is no definite or unqualified acceptance.

### **Resume**

Thus, a contract is always based upon:

- (i) Agreement (*consensus ad idem*) an unqualified acceptance of a definite offer;
- (ii) An intent to create legal obligations; and
- (iii) Consideration.

### **FLAWS IN CONTRACT**

There may be the circumstances under which a contract made under these rules may still be bad, because there is a flaw, vice or error somewhere. As a result of such a flaw, the apparent agreement is not a real agreement.

Where there is no real agreement, the law has three remedies:

*Firstly:* The agreement may be treated as of no effect and it will then be known as void agreement.

*Secondly:* The law may give the party aggrieved the option of getting out of his bargain, and the contract is then known as voidable.

*Thirdly:* The party at fault may be compelled to pay damages to the other party.

**(a) Void Agreement**

A void agreement is one which is destitute of all legal effects. It cannot be enforced and confers no rights on either party. It is really not a contract at all, it is non-existent. Technically the words 'void contract' are a contradiction in terms. But the expression provides a useful label for describing the situation that arises when a 'contract' is claimed but in fact does not exist. For example, a minors contract is void.

**(b) Voidable Contract**

A voidable contract is one which a party can put to an end. He can exercise his option, if his consent was not free. The contract will, however be binding, if he does not exercise his option to avoid it within a reasonable time. The consent of a party is not free and so he is entitled to avoid the contract, if he has given misrepresentation, fraud, coercion or undue influence.

**(c) Illegal Agreement**

An illegal agreement is one which, like the void agreement has no legal effects as between the immediate parties. Further, transactions collateral to it also become tainted with illegality and are, therefore, not enforceable. Parties to an unlawful agreement cannot get any help from a Court of law, for no polluted hands shall touch the pure fountain of justice. On the other hand, a collateral transaction can be supported by a void agreement.

For example, one party may have deceived the other party, or in some other way there may be no genuine consent. The parties may be labouring under a mistake, or one or both the parties may be incapable of making a contract. Again, the agreement may be illegal or physically impossible. All these are called "the FLAWS in contract or the *VICES* of contract".

The chief flaws in contract are:

- (i) Incapacity
- (ii) Mistake
- (iii) Misrepresentation
- (iv) Fraud
- (v) Undue Influence
- (vi) Coercion
- (vii) Illegality
- (viii) Impossibility.

**(i) Flaw in Capacity — Capacity and Persons**

In law, persons are either natural or artificial. Natural persons are human beings and artificial persons are corporations. Contractual capacity or incapacity is an incident of personality.

The general rule is that all natural persons have full capacity to make binding contracts. But the Indian Contract Act, 1872 admits an exception in the case of:

- (i) minors,
- (ii) lunatics, and
- (iii) persons disqualified from contracting by any law to which they are subject.

These persons are not competent to contract. Section 11 provides that 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". A valid agreement requires that both the parties should understand the legal implications of their conduct. Thus, both must have a mature mind. The legal yardstick to measure maturity according to the law of contract is, that both should be major and of sound mind and if not, the law would presume that the maturity of their mind has not reached to the extent of visualising the pros and cons of their acts, hence, a bar on minors and lunatics competency to contract.

The contractual capacity of a corporation depends on the manner in which it was created.

### Minor's Contract

According to the Indian Majority Act, 1875, a minor is a person, male or female, who has not completed the age of 18 years. In case a guardian has been appointed to the minor or where the minor is under the guardianship of the Court of Wards, the person continues to be a minor until he completes his age of 21 years. According to the Indian Contract Act, no person is competent to enter into a contract who is not of the age of majority. It was finally laid down by the Privy Council in the leading case of *Mohiri Bibi v. Dharmodas Ghose*, (1903) 30 Cal. 539, that a minor has no capacity to contract and minors contract is absolutely void. In this case, X, a minor borrowed Rs. 20,000 from Y, a money lender. As a security for the money advanced, X executed a mortgage in Y's favour. When sued by Y, the Court held that the contract by X was void and he cannot be compelled to repay the amount advanced by him.

Indian Courts have applied this decision to those cases where the minor has incurred any liability or where the liabilities on both sides are outstanding. In such cases, the minor is not liable. But if the minor has carried out his part of the contract, then, the Courts have held, that he can proceed against the other party. The rationale is to protect minors interest. According to the Transfer of Property Act, a minor cannot transfer property but he can be a transferee (person accepting a transfer). This statutory provision is an illustration of the above principle.

The following points must be kept in mind with respect to minors contract:

- A minor's contract is altogether void in law, and a minor cannot bind himself by a contract. If the minor has obtained any benefit, such as money on a mortgage, he cannot be asked to repay, nor can his mortgaged property be made liable to pay.
- Since the contract is void *ab initio*, it cannot be ratified by the minor on attaining the age of majority.
- Estoppel is an important principle of the law of evidence. To explain, suppose X makes a statement to Y and intends that the latter should believe and act upon it. Later on, X cannot rescile from this statement and make a new one.

In otherwords, X will be estopped from denying his previous statement. But a minor can always plead minority and is not estopped from doing so even where he had produced a loan or entered into some other contract by falsely representing that he was of full age, when in reality he was a minor.

But where the loan was obtained by fraudulent representation by the minor or some property was sold by him and the transactions are set aside as being void, the Court may direct the minor to restore the property to the other party.

For example, a minor fraudulently overstates his age and takes delivery of a motor car after executing a promissory note in favour of the trader for its price. The minor cannot be compelled to pay the amount to the promissory note, but the Court on equitable grounds may order the minor to return the car to the trader, if it is still with the minor.

Thus, according to Section 33 of the Specific Relief Act, 1963 the Court may, if the minor has received any benefit under the agreement from the other party require him to restore, so far as may be such benefit to the other party, to the extent to which he or his estate has been benefited thereby.

- (d) A minors estate is liable to pay a reasonable price for necessaries supplied to him or to anyone whom the minor is bound to support (Section 68 of the Act).

The necessaries supplied must be according to the position and status in life of the minor and must be things which the minor actually needs. The following have also been held as necessaries in India.

Costs incurred in successfully defending a suit on behalf of a minor in which his property was in jeopardy; costs incurred in defending him in a prosecution; and money advanced to a Hindu minor to meet his marriage expenses have been held to be necessaries.

- (e) An agreement by a minor being void, the Court will never direct specific performance of the contract.
- (f) A minor can be an agent, but he cannot be a principal nor can he be a partner. He can, however, be admitted to the benefits of a partnership.
- (g) Since a minor is never personally liable, he cannot be adjudicated as an insolvent.
- (h) An agreement by a parent or guardian entered into on behalf of the minor is binding on him provided it is for his benefit or is for legal necessity. For, the guardian of a minor, may enter into contract for marriage on behalf of the minor, and such a contract would be good in law and an action for its breach would lie, if the contract is for the benefit of the minor (*Rose Fernandez v. Joseph Gonsalves*, 48 Bom. L. R. 673) e.g., if the parties are of the community among whom it is customary for parents to contract marriage for their children. The contract of apprenticeship is also binding.

However, it has been held that an agreement for service, entered into by a father on behalf of his daughter who is a minor, is not enforceable at law (*Raj Rani v. Prem Adib*, (1948) 51 Bom. L.R. 256).

### **Lunatics Agreement (Section 2)**

A person of unsound mind is a lunatic. That is to say for the purposes of making contract, a person is of unsound mind if at the time when he makes the contract, he is incapable of understanding it and of forming rational judgment as to its effect upon his interests.

A person unsound mind cannot enter into a contract. A lunatics agreement is therefore void. But if he makes a contract when he is of sound mind, i.e., during lucid intervals, he will be bound by it.

A sane man who is delirious from fever, or who is so drunk that he cannot understand the terms of a contract, or form a rational judgement as to its effect on his interests cannot contract whilst such delirium or state of drunkenness lasts. A person under the influence of hypnotism is temporarily of unsound mind. Mental decay brought by old age or disease also comes within the definition.

Agreement by persons of unsound mind are void. But for necessaries supplied to a lunatic or to any member of his family, the lunatics estate, if any, will be liable. There is no personal liability incurred by the lunatic.

If a contract entered into by a lunatic or person of unsound mind is for his benefit, it can be enforced (for the benefit) against the other party (*Jugal Kishore v. Cheddu*, (1903) 1 All. L.J 43).

### **Persons Disqualified from Entering into Contract**

Some statutes disqualify certain persons governed by them, to enter into a contract. For example, Oudh Land Revenue Act provides that where a person in Oudh is declared as a 'disqualified proprietor under the Act, he is incompetent to alienate his property.

### **Alien Enemies**

A person who is not an Indian citizen is an alien. An alien may be either an alien friend or a foreigner whose sovereign or State is at peace with India, has usually contractual capacity of an Indian citizen. On the declaration of war between his country and India he becomes an alien enemy. A contract with an alien enemy becomes unenforceable on the outbreak of war.

For the purposes of civil rights, an Indian citizen of the subject of a neutral state who is *voluntarily* resident in hostile territory or is carrying on business there is an alien enemy. Trading with an alien enemy is considered illegal, being against public policy.

### **Foreign Sovereigns and Ambassadors**

Foreign sovereigns and accredited representatives of foreign states, i.e., Ambassadors, High Commissioners, enjoy a special privilege in that they cannot be sued in Indian Courts, unless they voluntarily submit to the jurisdiction of the Indian Courts. Foreign Sovereign Governments can enter into contracts through agents residing in India. In such cases the agent becomes personally responsible for the performance of the contracts.

### **Professional Persons**

In England, barristers-at law are prohibited by the etiquette of their profession from suing for their fees. So also are the Fellow and Members of the Royal College of Physicians and Surgeons. But they can sue and be sued for all claims other than their professional fees. In India, there is no such disability and a barrister, who is in the position of an advocate with liberty both to act and plead, has a right to contract and to sue for his fees (*Nihal Chand v. Dilawar Khan*, 1933 All. L.R. 417).

### **Corporations**

A corporation is an artificial person created by law, e.g., a company registered under the Companies Act, public bodies created by statute, such as Municipal Corporation of Delhi. A corporation exists only in contemplation of law and has no physical shape or form.

The Indian Contract Act does not speak about the capacity of a corporation to enter into a contract. But if properly incorporated, it has a right to enter into a contract. It can sue and can be sued in its own name. There are some contracts into which a corporation cannot enter without its seal, and others not at all. A company, for instance, cannot contract to marry. Further, its capacity and powers to contract are limited by its charter or memorandum of association. Any contract beyond such power is *ultra vires* and void.

### **Married Women**

In India there is no difference between a man and a woman regarding contractual capacity. A woman married or single can enter into contracts in the same ways as a man. She can deal with her property in any manner she likes, provided, of course, she is a major and is of sound mind.

Under the English law, before the passing of the Law Reform (Married Women and Tortfeasors) Act, 1935, a husband was responsible for his wife's contracts but since 1935 this liability no longer arises unless the wife

is acting as the husband's agent. Now, therefore, even in England a married woman has full contractual capacity, and can sue and be sued in her own name.

### Flaw in Consent

The basis of a contract is agreement, i.e., mutual consent. In other words, the parties should mean the same thing in the same sense and agree voluntarily. It is when there is consent, that the parties are said to be *consensus ad idem* i.e. their minds have met. Not only consent is required but it must be a free consent. Consent is not free when it has been caused by coercion, undue influence, misrepresentation, fraud or mistake. These elements if present, may vitiate the contract.

When this consent is wanting, the contract may turn out to be void or voidable according to the nature of the flaw in consent. Where there is no consent, there can be no contract as in the case of mutual mistake. Where there is consent, but it is not free, a contract is generally voidable at the option of the party whose consent is not free. In the case of misrepresentation, fraud, coercion, undue influence, the consent of one of the parties is induced or caused by the supposed existence of a fact which did not exist.

### (ii) Mistake (*Sections 20 and 21*)

The law believes that contracts are made to be performed. The whole structure of business depends on this as the businessmen depend on the validity of contracts. Accordingly, the law says that it will not aid any one to evade consequences on the plea that he was mistaken.

On the other hand, the law also realises that mistakes do occur, and that these mistakes are so fundamental that there may be no contract at all. If the law recognises mistake in contract, the mistake will render the contract void.

### Effect of Mistake

A mistake in the nature of miscalculation or error of judgement by one or both the parties has no effect on the validity of the contract. For example, if A pays an excessive price for goods under a mistake as to their true value, the contract is binding on him (*Leaf v. International Galleries* (1950) 1 All E.R. 693).

Therefore, mistake must be a "vital operative mistake", i.e. it must be a mistake of fact which is fundamental to contract.

To be operative so as to render the contract void, the mistake must be:

- (a) of fact, and not of law or opinion;
- (b) the fact must be essential to agreement, i.e., so fundamental as to negative the agreement; and
- (c) must be on the part of both the parties.

Thus, where both the parties to an agreement are under a mistake as to a matter of fact essential to agreement, the agreement is void (Section 20). Such a mistake prevents the formation of any contract at all and the Court will declare it void. For example, A agrees to buy from B a certain horse. It turns out that the horse was dead at the time of bargain though neither party was aware of the fact. The agreement is void.

### Mistake of Law and Mistake of Fact

Mistakes are of two kinds: (i) mistake of law, and (ii) mistake of fact. If there is a mistake of law of the land, the contract is binding because everyone is deemed to have knowledge of law of the land and ignorance of law is no excuse (*ignorantia juris non-excusat*).

But mistake of foreign law and mistake of private rights are treated as mistakes of fact and are excusable.

The law of a foreign country is to be proved in Indian Courts as ordinary facts. So mistake of foreign law makes the contract void. Similarly, if a contract is made in ignorance of private right of a party, it would be void, e.g., where A buys property which already belongs to him.

### **Mutual or Unilateral Mistake**

Mistake must be mutual or bilateral, i.e., it must be on the part of both parties. A unilateral mistake, i.e., mistake on the part of only one party, is generally of no effect unless (i) it concerns some fundamental fact and (ii) the other party is aware of the mistake. For this reason, error of judgement on the part of one of the parties has no effect and the contract will be valid.

### **Mutual or Common Mistake as to Subject-matter**

A contract is void when the parties to it assume that a certain state of things exist which does not actually exist or in their ignorance the contract means one thing to one and another thing to the other, and they contract subject to that assumption or under that ignorance. There is a mistake on the part of both the parties. Such a mistake may relate to the existence of the subject matter, its identity, quantity or quality.

- (a) *Mistake as to existence of the subject matter:* Where both parties believe the subject matter of the contract to be in existence but in fact, it is not in existence at the time of making the contract, there is mistake and the contract is void.

In *Couturier v. Hastie* (1857), there was a contact to buy cargo described as shipped from port A to port B and believed to be at sea which in fact got lost earlier unknown to the parties and hence not in existence at the time of the contract. Held, the contract was void due to the parties mistake.

- (b) *Mistake as to identity of the subject matter:* Where the parties are not in agreement to the identity of the subject matter, i.e., one means one thing and the other means another thing, the contract is void; there is no *consensus ad idem*.

In *Raffles v. Wichelhous* (1864), A agreed to buy from B a cargo of cotton to arrive "ex Peerless from Bombay". There were two ships called "Peerless" sailing from Bombay, one arriving in October and the other in December. A meant the earlier ship and B the latter. Held, the contract was void for mistake.

- (c) *Mistake as to quantity of the subject matter:* There may be a mistake as to quantity or extent of the subject matter which will render the contract void even if the mistake was caused by the negligence of a third-party.

In *Henkel v. Pape* (1870), P wrote to H inquiring the price of rifles and suggested that he might buy as many as fifty. On receipt of a reply he wired send three rifles. Due to the mistake of the telegraph clerk the message transmitted to H was send the rifles. H despatched 50 rifles. Held, there was no contract between the parties.

- (d) *Mistake as to quality of the subject-matter or promise:* Mistake as to quality raises difficult questions. If the mistake is on the part of both the parties the contract is void. But if the mistake is only on the part of one party difficulty arises.

The general rule is that a party to a contract does not owe any duty to the other party to disclose all the facts in his possession during negotiations. Even if he knows that the other party is ignorant of or under some misapprehension as to an important fact, he is under no obligation to enlighten him. Each party must protect his own interests unaided. In contract of sale of goods, this rule is summed up in the maxim *caveat emptor*.

*emptor* (Let the buyer beware.) The seller is under no duty to reveal the defects of his goods to the buyer, subject to certain conditions.

### Unilateral Mistake as to Nature of the Contract

The general rule is that a person who signs an instrument is bound by its terms even if he has not read it. But a person who signs a document under a fundamental mistake as to its nature (not merely as to its contents) may have it avoided provided the mistake was due to either-

- (a) the blindness, illiteracy, or senility of the person signing, or
- (b) a trick or fraudulent misrepresentation as to the nature of the document.

### Unilateral Mistake as to the Identity of the Person Contracted With

It is a rule of law that if a person intends to contract with A, B cannot give himself any right under it. Hence, when a contract is made in which personalities of the contracting parties are or may be of importance, no other person can interpose and adopt the contract. For example, where M intends to contract only with A but enters into contract with B believing him to be A, the contract is vitiated by mistake as there is no *consensus ad idem*.

Mistake as to the identity of the person with whom the contract is made will operate to nullify the contract only if:

- (i) the identity is for material importance to the contracts; and
- (ii) the mistake is known to the other person, i.e., he knows that it is not intended that he should become a party to the contract.

In *Cundy v. Lindsay* [(1878) 3 A.C. 459], one Blenkarn posing as a reputed trader Blankiron, placed an order for some goods with M/s Lindsay and Co. The company, thought that it is dealing with Blankiron and supplied the goods. Blenkarn sold the goods to Cundy and did not pay to Lindsay. The latter sued Cundy. The Court held that there was no contract between Lindsay and Blenkarn and therefore Cundy has no title to the goods.

### (iii) Misrepresentation (Section 18)

The term "misrepresentation" is ordinarily used to connote both "innocent misrepresentation" and "dishonest misrepresentation". Misrepresentation may, therefore, be either (i) Innocent misrepresentation, or (ii) Wilful misrepresentation with *intent to deceive* and is called fraud.

#### Innocent Misrepresentation

If a person makes a representation believing what he says is true he commits innocent misrepresentation. Thus, any false representation, which is made with an honest belief in its truth is innocent. The effect of innocent misrepresentation is that the party misled by it can avoid the contract, but cannot sue for damages in the normal circumstances.

But in order to avoid a contract on the ground of misrepresentation, it is necessary to prove that:

- (i) there was a representation or assertion,
- (ii) such assertion induced the party aggrieved to enter into the contract.
- (iii) the assertion related to a matter of fact ( and not of law as ignorance of law is no excuse).
- (iv) the statement was not a mere opinion or hearsay, or commendation (i.e., reasonable praise). For example an advertisement saying, "washes whiter than the whitest".

- (v) the statement which has become or turned out to be untrue, was made with an honest belief in its truth.

### **Damages for Innocent Misrepresentation**

Generally the injured party can only avoid the contract and cannot get damages for innocent misrepresentation. But in the following cases, damages are obtainable:

- (i) From a promoter or director who makes innocent misrepresentation in a company prospectus inviting the public to subscribe for the shares in the company;
- (ii) Against an agent who commits a breach of warranty of authority;
- (iii) From a person who (at the Courts discretion) is estopped from denying a statement he has made where he made a positive statement intending that it should be relied upon and the innocent party did rely upon it and thereby suffered damages;
- (iv) Negligent representation made by one person to another between whom a confidential relationship, like that of a solicitor and client exists.

### **(iv) Wilful Misrepresentation or Fraud (Section 17)**

Fraud is an untrue statement made knowingly or without belief in its truth or recklessly, carelessly, whether it be true or false with the intent to deceive. The chief ingredients of a fraud are:

- (i) a false representation or assertion;
- (ii) of fact (and not a mere opinion),
- (iii) made with the intention that it should be acted upon,
- (iv) the representation must have actually induced the other party to enter into the contract and so deceived him,
- (v) the party deceived must thereby be damaged, for there is no fraud without damages, and
- (vi) the statement must have been made either with the knowledge that it was false or without belief in its truth or recklessly without caring whether it was true or false.

It is immaterial whether the representation takes effect by false statement or with concealment. The party defrauded can avoid the contract and also claim damages.

Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless silence is in itself equivalent to speech, or where it is the duty of the person keeping silent to speak as in the cases of contracts *uberrimae fidei* - (contracts requiring utmost good faith).

### **Contracts Uberrimae Fidei**

There are contracts in which the law imposes a special duty to act with the utmost good faith i.e., to disclose all material information. Failure to disclose such information will render the contract voidable at the option of the other party.

### **Contracts *uberrimae fidei* are:**

- (a) *Contract of insurance of all kinds*: The assured must disclose to the insurer all material facts and whatever he states must be correct and truthful.
- (b) *Company prospectus*: When a company invites the public to subscribe for its shares, it is under

statutory obligation to disclose truthfully the various matters set out in the Companies Act. Any person responsible for non-disclosure of any of these matters is liable to damages. Also, the contract to buy shares is voidable where there is a material false statement or non-disclosure in the prospectus.

- (c) *Contract for the sale of land:* The vendor is under a duty to the purchaser to show good title to the land he has contracted to sell.
- (d) *Contracts of family arrangements:* When the members of a family make agreements or arrangements for the settlement of family property, each member of the family must make full disclosure of every material fact within his knowledge.

#### **Difference between Fraud and Innocent Misrepresentation**

1. Fraud implies an intent to deceive, which is lacking if it is innocent misrepresentation.
2. In case of misrepresentation and fraudulent silence, the defendant can take a good plea that the plaintiff had the means of discovering the truth with ordinary diligence. This argument is not available if there is fraud (Section 19- exception).
3. In misrepresentation the plaintiff can avoid or rescind the contract. In fraud, the plaintiff can claim damages as well.
4. If there is fraud, it may lead to prosecution for an offence of cheating under the Indian Penal Code.

#### **(v) Coercion**

Coercion as defined in Section 15 means “the committing or threatening to commit any act forbidden by the Indian Penal Code, or unlawful detaining or threatening to detain, any property to the prejudice of any person whatever with the intention of causing any person to enter into an agreement”. Simply stated, the doing of any act forbidden by the Indian Penal Code is coercion even though such an act is done in a place where the Indian Penal Code is not in force. If A at the point of a pistol asks B to execute a promissory note in his favour and B to save his life does so he can avoid this agreement as his consent was not free. Even a threat to third-party, e.g., where A compels B to sign a document threatening to harm C, in case B does not sign would also amount to coercion.

It has been held that mere threat by one person to another to prosecute him does not amount to coercion. There must be a contract made under the threat and that contract should be one sought to be avoided because of coercion (*Ramchandra v. Bank of Kohlapur*, 1952 Bom. 715). It may be pointed out that coercion may proceed from any person and may be directed against any person, even a stranger and also against goods, e.g., by unlawful detention of goods.

#### **(vi) Undue Influence**

Under Section 16 of the Indian Contract Act, 1872, a contract is said to be produced by undue influence “where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other”.

The elements of undue influence are (i) a dominant position, and (ii) the use of it to obtain an unfair advantage. The words “unfair advantage” do not limit the jurisdiction to cases where the transaction would be obviously unfair as between persons dealing on an equal footing. In the words of Lord Kingston, “the principle applies to every case where influence is acquired and abused where confidence is reposed and betrayed”.

Sub-section (2) of Section 16 provides that a person is deemed to be in a position to dominate the will of another—

- (a) Where he holds a real or apparent authority over the other or where he stands in a fiduciary relation to the other, e.g., minor and guardian; trustee and beneficiary; solicitor and client. There is, however, no presumption of undue influence in the relation of creditor and debtor, husband and wife (unless the wife is a *parda-nishin* woman) and landlord and tenant. In these cases the party has to prove that undue influence has been exercised on him, there being no presumption as to existence of undue influence.
- (b) Where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness or mental or bodily distress e.g., doctor and patient.

### Illustration

A, having advanced money to his son B, during his minority, upon B's coming of age obtains, by misuse of parental influence a bond upon B for a greater amount than the sum due in respect of the advance. A employs undue influence.

A, a man enfeebled by disease or age is induced by B's influence over him as his medical attendant, to agree to pay B an unreasonable sum for his professional services. B employs undue influence.

A parent stands in a fiduciary relation towards his child and any transaction between them by which any benefit is procured by the parent to himself or to a third party, at the expense of the child will be viewed with jealousy by Courts of Equity and the burden will be on the parent or third-party claiming the benefit of showing that the child while entering into the transaction had independent advice, that he thoroughly understood the nature of transaction and that he was removed from all undue influence when the gift was made (*Marim Bibi v. Cassim Ebrahim* (1939) 184 I.C. 171 (1939) A.I.R. 278).

Where there is a presumption of undue influence, the presumption can be rebutted by showing that

- (i) full disclosure of all material facts was made,
- (ii) the consideration was adequate, and
- (iii) the weaker party was in receipt of independent legal advice.

### Transaction with *parda-nishin* women

The expression '*parda-nishin*' denotes complete seclusion. Thus, a woman who goes to a Court and gives evidence, who fixes rents with tenants and collects rents, who communicates when necessary, in matters of business, with men other than members of her own family, could not be regarded as a *parda-nishin* woman (*Ismail Musafee v. Hafiz Boo* (1906) 33 Cal. LR 773 and 33 I.A. 86). The principles to be applied to transactions with *parda-nishin* woman are founded on *equity and good conscience* and accordingly a person who contracts with *parda-nishin* woman has to prove that no undue influence was used and that she had free and independent advice, fully understood the contents of the contract and exercised her free will. "The law throws around her a special cloak of protection" (*Kali Baksh v. Ram Gopal* (1914) L.R. 41 I.A. 23, 28-29, 36 All 81, 89).

**Unconscionable transactions:** An unconscionable transaction is one which makes an exorbitant profit of the others distress by a person who is in a dominant position. Merely the fact that the rate of interest is very high in a money lending transaction shall not make it unconscionable. But if the rate of interest is very exorbitant and the Court regards the transaction unconscionable, the burden of proving that no undue influence was exercised lies on the creditor. It has been held that urgent need of money on the part of the borrower does

not itself place the lender in a position to dominate his will within the meaning of this Section (Sunder Koer v. Rai Sham Krishen (1907) 34 Cal. 150, C.R. 34 I.A. 9).

### (vii) Legality of Object

One of the requisites of a valid contract is that the object should be lawful. Section 10 of the Indian Contract Act, 1872, provides, "All agreements are contracts if they are made by free consent of parties competent to contract *for a lawful consideration and with a lawful object...*" Therefore, it follows that where the consideration or object for which an agreement is made is unlawful, it is not a contract.

Section 23 of the Indian Contract Act, 1872 provides that the consideration or object of an agreement is lawful unless it is

- (i) forbidden by law; or
- (ii) it is of such nature that if permitted it would defeat the provisions of law; or
- (iii) is fraudulent; or
- (iv) involves or implies injury to the person or property of another; or
- (v) the Court regards it an immoral or opposed to public policy.

In each of these cases the consideration or object of an agreement is said to be unlawful. *Every agreement of which the object or consideration is unlawful is void.*

### Illustration

- (i) X, Y and Z enter into an agreement for the division among them of gains acquired by them by fraud. The agreement is void as its object is unlawful.
- (ii) X promises to obtain for Y an employment in the Government service and Y promises to pay Rs. 1,500 to X. The agreement is void, as the consideration for it is unlawful.
- (iii) X promises to Y to drop a prosecution which he has instituted against Y for robbery, and Y promises to restore the value of the things taken. The agreement is void as its object is unlawful.
- (iv) A who is B's *mukhtr* promises to exercise his influence, as such, with B in favour of C and C promises to pay Rs. 1,000 to A. The agreement is void because it is immoral.
- (v) An agreement by the proprietors of a newspaper to indemnify the printers against claims arising from libels printed in the newspaper is void as it implies or involves injury to the person of another.

### Void and Illegal Contracts

A void contract is one which is destitute of legal effects altogether. An illegal contract too has no legal effect as between the immediate parties to the contract, but has the further effect of tainting the collateral contracts also with illegality. For instance A borrows from B to Rs. 1,000 for lending to C a minor. The contract between A and C is void, but B can nevertheless recover the money from A. On the other hand, if A had borrowed Rs. 1,000 from B to buy a pistol to shoot C, the question whether B can recover the money hinges on whether B was aware of the purpose for which money was borrowed. If B had knowledge of the illegal purpose, he cannot recover. Therefore, it may be said that *all illegal agreements are void but all void agreements are not necessarily illegal.*

### Consequence of Illegal Agreements

- (i) an illegal agreement is entirely void;
- (ii) no action can be brought by a party to an illegal agreement. The maxim is "*Ex turpi cause non-oritur action*" - from an evil cause, no action arises;

- (iii) money paid or property transferred under an illegal agreement cannot be recovered. The maxim is *in parti delicto potier est conditio defendentis* - In cases of equal guilt, more powerful is the condition of the defendant;
- (iv) where an agreement consist of two parts, one part legal and other illegal, and the legal parts is separable from the illegal one, then the Court will enforce the legal one. If the legal and the illegal parts cannot be separated the whole agreement is illegal; and
- (v) any agreement which is collateral to an illegal agreement is also tainted with illegality and is treated as being illegal, even though it would have been lawful by itself (*Film Pratapchand v. Firm Kotri Re.* AIR (1975) S.C. 1223).

### Exception to General Rule of no Recovery of Money or Property

In the following cases, a party to an illegal agreement may sue to recover money paid or property transferred:

- (a) Where the transfer is not in *pari delicto* (equally guilty) with the defendant, i.e. the transferee. For example, where A is induced to enter into an illegal agreement by the fraud of B, A may recover the money paid if he did not know that the contract was illegal.
- (b) If the plaintiff can frame a cause of action entirely dependent of the contract.
- (c) Where a substantial part of the illegal transaction has not been carried out and the plaintiff is truly and genuinely repentant. (*Bigos v. Bonstead* (1951), All E.R. 92).

### Agreements Void as being Opposed to Public Policy

The head public policy covers a wide range of topics. Agreements may offend public policy by tending to the prejudice of the State in times of war, by tending to the abuse of justice or by trying to impose unreasonable and inconvenient restrictions on the free choice of individuals in marriage, or their liberty to exercise lawful trade or calling. The doctrine of public policy is a branch of Common Law and like any other branch of Common Law it is governed by the precedents [*Gherulal Parakh v. Mahadeodas Maiya* (1959) 2 S.C.R. (Suppl.) 406; AIR 1959 S.C. 781]. The doctrine of public policy is not to be extended beyond the classes of cases already covered by it and no Court can invent a new head of public policy [*Lord Halsbury, Janson v. Driefontien Consolidated Mines* (1902) A.C. 484, 491]. It has been said by the House of Lords that public policy is always an unsafe and treacherous ground for legal decisions. Even if it is possible for Courts to evolve a new head of public policy, it should be done under extraordinary circumstances giving rise to incontestable harm to the society.

The following agreement are void as being against public policy but they are not illegal:

- (a) *Agreement in restraint of parental rights*: An agreement by which a party deprives himself of the custody of his child is void.
- (b) *Agreement in restraint of marriage*: An agreement not to marry at all or not to marry any particular person or class of persons is void as it is in restraint of marriage.
- (c) *Marriage brocage or brokerage Agreements*: An agreement to procure marriage for reward is void. Where a purohit (priest) was promised Rs. 200 in consideration of procuring a wife for the defendant, the promise was held void as opposed to public policy, and the purohit could not recover the promised sum.
- (d) *Agreements in restraint of personal freedom are void*: Where a man agreed with his money lender not to change his residence, or his employment or to part with any of his property or to incur any obligation on credit without the consent of the money lender, it was held that the agreement was void.

- (e) *Agreement in restraint of trade:* An agreement in restraint of trade is one which seeks to restrict a person from freely exercising his trade or profession.

## AGREEMENTS IN RESTRAINT OF TRADE VOID

Section 27 of the Indian Contract Act states that every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is, to that extent, void.

This Section is not happily worded and has been criticised by many authors. It appears from the wording that every kind of restraint, whether total or partial falls within the prohibition of this Section. In English law the Courts have held that if a restraint is reasonable, it will be valid. Leading case on this point is *Nordenfelt v. Maxim Nordenfelt Guns Co.*, (1894) A.C. 535. N was an inventor and a manufacturer of guns and ammunition. He sold his world-wide business to M and promised not to manufacture guns anywhere in the world for 25 years. The House of Lords held that the restraint was reasonable as it was no more than is necessary for the protection of the company, the contract was binding. Whether a restraint is reasonable or not depends upon the facts of each case.

Our courts are not consistent on the point whether reasonable restraints are permitted or not. In *Madhub Chunder v. RaCoomar* (1874) 14 Bang. L.R. 76, A paid Rs. 900 to B's workman. B undertook to stop his business in a particular locality in Calcutta. He did not keep his promise. A's suit for the sum was dismissed since the agreement was void under Section 27. The reasonableness or otherwise of the restraint was not discussed. However, if a restrictive meaning is adopted, most of the ordinary mercantile agreements may be hit. Thus, the Courts have held that if the restraint is one which is really necessary for the carrying on business, the same is not prohibited. In *Mackenzie v. Sitarmiah*, (1891) 15 Mad. 79, A agreed to sell to B all the salt he manufactured and B agreed to buy such salt. A further agreed not to sell salt to third-parties. The Court held that the agreement was valid.

Other type of restraints are personal covenants between an employer and his employee whereby the latter agrees not to compete with the former or serve with any of his competitors after employment. This issue came before the Supreme Court in *Niranjan Shanker Golikari v. The Century Spinning and Manufacturing Co. Ltd.*, AIR 1967 S.C. 1098. In this case N entered into a bond with the company to serve for a period of five years. In case, N leaves his job earlier and joins elsewhere with company's competitor within five years, he was liable for damages. N was imparted the necessary training but he left the job and joined another company. The former employer instituted a suit against N. The Supreme Court, held that the restraint was necessary for the protection of the company's interests and not such as the Court would refuse to enforce.

In other case, it has been reiterated that the restriction should be reasonable taking into account the facts and circumstances of the case. In *Superintendence Company of India Ltd. v. Krishna Murgai* [(1981) 2 SCC 246], the Supreme Court laid down that a restraint beyond the term of service would be void and the only ground on which it can be justified is by showing it is necessary for the protection of the employer's goodwill.

The words "to the extent" in Section 27 make it clear that if in an agreement there are some covenants which are prohibited whereas the others are not and if the two parts can be separated then only those covenants which operate as restraint of trade would be void and not whole of the agreement itself. To illustrate, in *Brahmputra Tea Co. Ltd. v. Scarth* (1885) I.L.R. Cal. 545, the employee agreed with the employer firstly, not to compete with latter after leaving the job and, secondly, not to injure employer's interest during employment. The Court held that the first condition is a restraint of trade but the second is binding.

## When Contracts in Restraint of Trade Valid

*Prima facie* every restraint of trade is void, but certain exceptions to this general rule are recognised. If a

partial and reasonable restraint falls under any of the following exceptions, the contract will be enforceable:

- (a) *Sale of goodwill*: Where the seller of the goodwill of a business undertakes not to compete with the purchaser of the goodwill, the contract is enforceable provided the restraint appears to be reasonable as to territorial limits and the length of time.
- (b) *Partners agreements*: Section 11(2) of the Indian Partnership Act permits contracts between partners to provide that a partner shall not carry on any business other than that of the firm while he is a partner.
- (c) Section 36(2) and Section 54 of the Indian Partnership Act provide that a partner may make an agreement with his partners that on ceasing to be a partner he will not carry on any business similar to that of the firm within specified period or within specified limits. The agreement shall be binding if the restrictions are reasonable.

*Trade Combinations*: An agreement, the object of which is to regulate business and not to restrain it is valid. Thus, an agreement in the nature of a business combination between traders or manufacturers e.g. not to sell their goods below a certain price, to pool profits or output and to divide the same in an agreed proportion does not amount to a restraint of trade and is perfectly valid (*Fraster & Co. v. Laxmi Narain*, (1931) 63 All 316).

*Negative stipulations in service agreements*: An agreement of service by which a person binds himself during the term of the agreement not to take service with anyone else is not in restraint of lawful profession and is valid.

## **WAGERING AGREEMENTS**

The literal meaning of the word “wager” is a “bet”. Wagering agreements are nothing but ordinary betting agreements. For example, A and B enter into an agreement that if England’s Cricket Team wins the test match, A will pay B Rs. 100 and if it loses B will pay Rs. 100 to A. This is a wagering agreement and nothing can be recovered by winning party under the agreement.

The essence of gaming and wagering is that one party is to win and the other to lose upon a future event which at the time of the contract is of an uncertain nature that is to say, if the event turns out one way A will lose; but if it turns out the other way he will win (*Thacker v. Hardy*, (1878) 4 OBD 685).

### **Wagering Agreements Void**

In India except Mumbai, wagering agreements are void. In Mumbai, wagering agreements have been declared illegal by the Avoiding Wagers (Amendment) Act, 1865. Therefore, in Mumbai a wagering agreement being illegal, is void not only between the immediate parties, but taints and renders void all collateral agreements to it.

Thus, A bets with B and loses, applies to C for a loan, who pays B in settlement of A’s losses. C cannot recover from A because this is money paid “under” or “in respect of” a wagering transaction which is illegal in Mumbai. But in respect of India such a transaction (i.e., betting) being only void, C could recover from A. Of course, if A refused to pay B the amount of the bet that he has lost, B could not sue A anywhere. Again, where an agent bets on behalf of his principal and loses and pays over the money to the winner, he cannot recover the money from his principal, if the transaction took place in Mumbai, but elsewhere he could recover. But if the agent wins, he must pay the winnings to the principal, as this money was received on behalf of the principal.

Sometimes, commercial transactions assume the form of wagering contracts. The sample test to find out whether a particular transaction is a wager or a genuine commercial transaction is: “Where delivery of the

goods sold is intended to be given and taken, it is valid contract, but where only the differences are intended to be paid, it will be a wagering contract and unenforceable".

In a wagering contract there must be mutuality in the sense that the gain of one party should be loss to the other on the happening of an uncertain event which is the subject matter of the contract.

## VOID AGREEMENTS

The following types of agreements are void under Indian Contract Act:

- (a) Agreement by or with a minor or a person of unsound mind or a person disqualified to enter into a contract - Section 11;
- (b) Agreement made under a mistake of fact, material to the agreement on the part of the both the parties - Section 20.
- (c) An agreement of which the consideration or object is unlawful - Section 23.
- (d) If any part of a single consideration for one or more objects, or any one or any part of any one of several considerations for a single object, is unlawful, the agreement is void - Section 24.
- (e) An agreement made without consideration subject to three exceptions provided to Section 25.
- (f) An agreement in restraint of marriage - Section 26.
- (g) An agreement in restraint of trade - Section 27.
- (h) An agreement in restraint of legal proceedings - Section 28.
- (i) Agreements, the meaning of which is not certain, or capable of being made certain - Section 29.
- (j) Agreement by way of wager- Section 30.
- (k) An agreement to enter into an agreement in the future.
- (l) An agreement to do an act impossible in itself - Section 56(1)

## When contract becomes void

An agreement not enforceable by law is void *ab initio* - Section 2(g).

A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable - Section 2(j)

A contract becomes void when, by reason of some event which the promisor could not prevent, the performance of the contract becomes impossible, e.g., by destruction of the subject- matter of the contract after the formation of the contract.

A contract becomes void by reason of subsequent illegality. A in India agrees to supply goods to B in Pakistan. After the formation of the contract war breaks out between India and Pakistan and the supply of goods to Pakistan is prohibited by legislation. The contract becomes void.

A contingent contract to do or not do to anything if an uncertain future event happens becomes void if the event becomes impossible.

Where a contract is voidable at the option of the aggrieved party, the contract becomes void when the option is exercised by him.

## RESTITUTION

When a contract becomes void, it is not to be performed by either party. But if any party has received any benefit under such a contract from the other party he must restore it or make compensation for it to the other party. A agrees to sell to B after 6 months a certain quantity of gold and receives Rs 500 as advance. Soon after the agreement, private sales of gold are prohibited by law. The contract becomes void and A must return the sum of Rs. 500 to B.

Restitution is also provided for by Section 65 where an agreement is discovered to be void. A pays Rs. 500 in consideration of B's promising to marry, C, A's daughter C is dead at the time of the promise. The agreement is discovered to be void and B must pay back Rs. 500.

But there is no resolution where the parties are wholly incompetent to contract, e.g., where one of the parties is a minor. The minor cannot be asked to restore the benefit, e.g., a minor borrowed Rs. 1,000 from B, he cannot be asked to pay back Rs. 1,000 to B because the contract is void (*Mohiri Bibis* case).

## CONTINGENT CONTRACT (Section 31)

As per Section 31, a contingent contract is a contract to do or not to do something, if some event *collateral to such contract*, does or does not happen. For example, A contracts to sell B 10 bales of cotton for Rs. 20,000, if the ship by which they are coming returns safely. This is a contingent contract.

Contract of insurance and contracts of indemnity and guarantee are popular instances of contingent contracts.

### Rules regarding contingent contracts

The following rules are contained in Section 32-36:

- (a) Contracts contingent upon the happening of a future uncertain event cannot be enforced by law unless and until that event has happened. If the event becomes impossible, the contract becomes void - Section 32.
  - (i) A makes a contract to buy B's house if A survives C. This contract cannot be enforced by law unless and until C dies in A's lifetime.
  - (ii) A contracts to pay B a sum of money when B marries C, C dies without being married to B. The contract becomes void.
- (b) Contracts contingent upon the non-happening of an uncertain future event can be enforced when the happening of that event becomes impossible and not before - Section 33.
 

A contracts to pay B a certain sum of money if a certain ship does not return. The ship is sunk. The contract can be enforced when the ship sinks.
- (c) If a contract is contingent upon how a person will act at an unspecified time, the event shall be considered to become impossible when such person does anything which renders it impossible that he should so act within any definite time or otherwise than under further contingencies - Section 34.
 

A agrees to pay B Rs. 1,000 if B marries C. C marries D. The marriage of B to C must now be considered impossible although it is possible that D may die and C may afterwards marry B.
- (d) Contracts contingent on the happening of an event within a fixed time become void if, at the expiration of the time, such event has not happened, or if, before the time fixed, such event becomes impossible - Section 35.

A promises to pay B a sum of money if a certain ship returns within a year. The contract may be enforced if the ship returns within the year, and becomes void if the ship is burnt within the year.

- (e) Contracts contingent upon the non-happening of an event within a fixed time may be enforced by law when the time fixed has expired and such event has not happened or before the time fixed has expired, if it becomes certain that such event will not happen - Section 35

A promises to pay B a sum of money if a certain ship does not return within the year. The contract may be enforced if the ship does not return within the year or is burnt within the year.

- (f) Contingent agreements to do or not to do anything if an impossible event happens, are void, whether the impossibility of the event is known or not known to the parties to the agreement at the time when it is made - Section 36.

A agrees to pay Rs. 1,000 to B if two straight lines should enclose a space. The agreement is void.

## CERTAIN RELATIONS RESEMBLING THOSE OF CONTRACT (QUASI CONTRACTS)

### Nature of Quasi-Contracts

A valid contract must contain certain essential elements, such as offer and acceptance, capacity to contract, consideration and free consent. But sometimes the law implies a promise imposing obligations on one party and conferring right in favour of the other even when there is no offer, no acceptance, no *consensus ad idem*, and in fact, there is neither agreement nor promise. Such cases are not contracts in the strict sense, but the Court recognises them as relations resembling those of contracts and enforces them as if they were contracts, hence the term quasi- contracts (i.e., resembling a contract).

A quasi-contract rests on the equitable principle that a person shall not be allowed to enrich himself unjustly at the expense of another. In truth, it is not a contract at all. It is an obligation which the law creates, in the absence of any agreement, when any person is in the possession of one persons money, or its equivalent, under such circumstances that in equity and good conscience he ought not to retain it, and which in justice and fairness belongs to another. It is the duty and not an agreement or intention which defines it. A very simple illustration is money paid under mistake. Equity demands that such money must be paid back.

### Quasi-Contracts or Implied Contracts under the Indian Contract Act

The following types of quasi-contracts have been dealt within the Indian Contract Act—

- (a) Necessaries supplied to person incapable of contracting or to anyone whom he is illegally bound to support - Section 68.
- (b) Suit for money had and received - Section 69 and 72.
- (c) *Quantum Meruit*
- (d) Obligations of a finder of goods - Section 71.
- (e) Obligation of person enjoying benefit of a non-gratuitous act - Section 70

### Necessaries

Contracts by minors and persons of unsound mind are void. However, Section 68 of the Indian Contract Act provides that their estates are liable to reimburse the trader, who supplies them with necessities of life.

### Suit for money had and received

The right to file a suit for the recovery of money may arise

- (a) *Where the plaintiff paid money to the defendant* (i) under a mistake, (ii) in pursuance of a contract

the consideration for which has failed, or (iii) under coercion, oppression, extortion or other such means.

A debtor may recover, from a creditor the amount of an over-payment made to him by mistake. The mistake may be mistake of fact or a mistake of law.

- (b) *Payment to third-party of money which another is bound to pay.* For example, where A's goods are wrongfully attached in order to realise arrears of Government revenue due by B, and A pays the amount to save his goods from being sold, he is entitled to recover the amount from B.
- (c) *Money obtained by defendant from third-parties.* For example, where an agent has obtained a secret commission or a fraudulent payment from a third-party, the principle can recover the amount from the agent.

### Quantum Meruit

The expression “*Quantum Meruit*” literally means “as much as earned” or reasonable remuneration. It is used where a person claims reasonable remuneration for the services rendered by him when there was no express promise to pay the definite remuneration. Thus, the law implies reasonable compensation for the services rendered by a party if there are circumstances showing that these are to be paid for.

The general rule is that where a party to a contract has not fully performed what the contract demands as a condition of payment, he cannot sue for payment for that which he has done. The contract has to be indivisible and the payment can be demanded only on the completion of the contract.

But where one party who has performed part of his contract is prevented by the other from completing it, he may sue on a *quantum meruit*, for the value of what he has done.

The claim on a *quantum meruit* arises when one party abandons the contract, or accepts the work done by another under a void contract.

The party in default may also sue on a “*quantum meruit*” for what he has done if the contract is divisible and the other party has had the benefit of the part which has been performed. But if the contract is not divisible, the party at fault cannot claim the value of what he has done.

### Obligations of finder of lost goods

The liability of a finder of goods belonging to someone else is that of a bailee. This means that he must take as much care of the goods as a man of ordinary prudence would take of his own goods of the same kind. So far as the real owner of the goods is concerned, the finder is only a bailee and must not appropriate the goods to his own use. If the owner is traced, he must return the goods to him. The finder is entitled to get the reward that may have been offered by the owner and also any expenses he may have incurred in protecting and preserving the property.

### Obligation of a person enjoying benefit of non-gratuitous act

Section 70 of the Indian Contract Act provides that where a person lawfully does something for another person or delivers anything to him without any intention of doing so gratuitously and the other person accepts and enjoys the benefit thereof, the latter must compensate the former or restore to him the thing so delivered. For example, when one of the two joint tenants pays the whole rent to the landlord, he is entitled to compensation from his co-tenant, or if A, a tradesmen, leaves goods at B's house by mistake and B treats the goods as his own, he is bound to pay A for them.

## DISCHARGE OR TERMINATION OF CONTRACTS

A contract is said to be discharged or terminated when the rights and obligations arising out of a contract are extinguished.

Contracts may be discharged or terminated by any of the following modes:

- (a) performance, i.e., by fulfilment of the duties undertaken by parties or, by tender;
- (b) mutual consent or agreement.
- (c) lapse of time;
- (d) operation of law;
- (e) impossibility of performance; and
- (f) breach of contract.

### (a) Performance of Contracts (Section 37)

Section 37 of the Act provides that the parties to a contract must either perform or offer to perform their respective promises, unless such performance is dispensed with or excused under the provision of the Indian Contract Act, or any other law. In case of death of the promisor before performance, the representatives of the promisor are bound to perform the promise *unless a contrary intention appears from the contract.*

#### Illustration

X promises to deliver a horse to Y on a certain day on payment of Rs 1,000. X dies before that day. X's representatives are bound to deliver the horse to Y and Y is bound to pay Rs. 1,000 to X's representatives.

### Tender of Performance (Section 38)

In case of some contracts, it is sometimes sufficient if the promisor performs his side of the contract. Then, if the performance is rejected, the promisor is discharged from further liability and may sue for the breach of contract if he so wishes. This is called discharge by tender.

To be valid, a tender must fulfil the following conditions

- (a) it must be unconditional;
- (b) if must be made at a proper time and place;
- (c) it must be made under circumstances enabling the other party to ascertain that the party by whom it is made is able and willing then and there to do the whole of what he is bound, to do by his promise;
- (d) if the tender relates to delivery of goods, the promisee must have a reasonable opportunity of seeing that the thing offered is the thing which the promisor is bound by his promise to deliver;
- (e) tender made to one of the several joint promisees has the same effect as a tender to all of them.

### Who can demand performance?

Generally speaking, a stranger to contract cannot sue and the person who can demand performance is the party to whom the promise is made. But an assignee of the rights and benefits under a contract may demand performance by the promisor, in the same way as the assignor, (i.e., the promisee) could have demanded.

### Effect of refusal of party to perform wholly

Section 39 provides that when a party to a contract has refused to perform or disabled himself from

performing his promise in its entirety, the promisee may put an end to the contract unless he had signified by words or conduct his acquiescence in its continuance.

### Illustration

- (a) X, a singer enters into a contract with Y, the manager of a theatre to sing at his theatres two nights in every week during the next two months, and Y engaged to pay her Rs. 100 for each nights performance. On the sixth night X wilfully absents herself from the theatre. Y is at liberty to put an end to the contract.
- (b) If in the above illustration, with the assent of Y, X sings on the seventh night, Y is presumed to have signified his acquiescence in the continuance of the contract and cannot put an end to it; but is entitled to compensation for the damages sustained by him through X's failure to sing on the sixth night.

### By whom contract must be performed

Under Section 40 of the Act, if it appears from the nature of the case that it was the intention of the parties to a contract that it should be performed by the promisor himself such promise must be performed by the promisor himself. In other cases, the promisor or his representative may employ a competent person to perform it.

### Illustration

- (a) X promises to pay Rs. 1,000 to Y. X may either personally pay the money to Y or cause it to be paid to Y by another. If X dies before making payment, his representatives must perform the promise or employ some proper person to do so.
- (b) X promises to paint a picture for Y. X must personally perform the promise.

### Devolution of Joint Liabilities

Under Section 42 of the Indian Contract Act, where two or more persons have made a joint promise then, *unless a contrary intention appears* from the contract all such persons should perform the promise. If any one of them dies, his representatives jointly with the survivor or survivors should perform. After the death of the last survivor, the representatives of all jointly must fulfil the promise.

Under Section 43 of the Indian Contract Act when two or more persons made a joint promise, the promisee may, in the *absence of an express agreement* to the contrary compel any one or more of such joint promisors to perform the whole of the promise. Each of two or more joint promisors may compel every other joint promisor to contribute equally with himself to the performance of the promise *unless a contrary intention appears from the contract*. If any one of two or more promisors make default in such contribution, the remaining joint promisors should bear the loss arising from such default in equal share.

### Illustrations

- (a) X, Y and Z jointly promise to pay Rs. 6,000 to A. A may compel either X or Y or Z to pay the amount.
- (b) In the above example imagine, Z is compelled to pay the whole amount; X is insolvent but his assets are sufficient to pay one-half of his debts. Z is entitled to receive Rs. 1,000 from X's estate and Rs. 2,500 from Y.
- (c) X, Y and Z make a joint promise to pay Rs. 5,000 to A, Z is unable to pay any amount and X is compelled to pay the whole. X is entitled to receive Rs. 3,000 from Y.

Under Section 44 of the Act, where two or more persons have made a joint promise, a release of one of such

joint promisors by the promisee does not discharge the other joint promisor(s); neither does it free the joint promisor so released from responsibility to the other joint promisor or joint promisors.

### Devolution of Joint Rights

A promise may be made to two or more persons. The promisees are called joint promisees. For example, X may give a promise to repay Rs. 1,000 given by Y and Z jointly. In such case, *in the absence of a contrary intention*, the right to claim, performance rests with Y and Z. If Y dies, Y's representative jointly with Z may, demand performance. If Z also dies, the representatives of Y and Z may demand jointly performance from X.

### Assignment

The promisee may assign rights and benefits of contract and the assignee will be entitled to demand performance by the promisor. But the assignment to be complete and effectual, must be made by an instrument in writing.

An obligation or liability under a contract cannot be assigned. For example, if A owes B Rs. 500 and A transfers the liability to C i.e. asks C to pay the sum to B, this would not bind B, and B may not consent to this arrangement, as he may know nothing of C's solvency. But if B consents to accept performance by C, there is a substitution of new contract and the old contract is discharged and all rights and liabilities under it are extinguished. This is technically called *novation*.

### (b) Discharge by Mutual Agreement or Consent (Sections 62 and 63)

A contract may be discharged by the agreement of all parties to the contract, or by waiver or release by the party entitled to performance.

The methods stipulated under Sections 62 and 63 of the Indian Contract Act for discharging a contract by mutual consent are:

*Novation* — when a new contract is substituted for existing contract either between the same parties or between different parties, the consideration mutually being the discharge of the old contract.

*Alteration* — change in one or more of the material terms of a contract.

*Rescission* — by agreement between the parties at any time before it is discharged by performance or in some other way.

*Remission* — acceptance of a lesser sum than what was contracted for or a lesser fulfilment of the promise made.

*Waiver* — deliberate abandonment or giving up of a right which a party is entitled to under a contract, whereupon the other party to the contract is released from his obligation.

### (c) Discharge by Lapses of Time

The Limitation Act, in certain circumstance, affords a good defence to suits for breach of contract, and infact terminates the contract by depriving the party of his remedy to law. For example, where a debtor has failed to repay the loan on the stipulated date, the creditor must file the suit against him within three years of the default. If the limitation period of three years expires and he takes no action he will be barred from his remedy and the other party is discharged of his liability to perform.

### (d) Discharge by Operation of the Law

Discharge under this head may take place as follows:

- (a) *By merger*: When the parties embody the inferior contract in a superior contract.

- (b) *By the unauthorised alteration of items of a written document:* Where a party to a written contract makes any material alteration without knowledge and consent of the other, the contract can be avoided by the other party.
- (c) *By insolvency:* The Insolvency Act provides for discharge of contracts under particular circumstances. For example, where the Court passes an order discharging the insolvent, this order exonerates or discharges him from liabilities on all debts incurred previous to his adjudication.

#### **(e) Discharge by Impossibility or Frustration (Section 56)**

A contract which is entered into to perform something that is clearly impossible is void. For instance, A agrees with B to discover treasure by magic. The agreement is void by virtue of Section 56 para 1 which lays down the principle that an agreement to do an act impossible in itself is void.

Sometimes subsequent impossibility (i.e. where the impossibility supervenes after the contract has been made) renders the performance of a contract unlawful and stands discharged; as for example, where a singer contracts to sing and becomes too ill to do so, the contract becomes void. In this connection, para 2 of Section 56 provides that a contract to do an act, which after the contract is made, becomes impossible or by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.

If the impossibility is not obvious and the promisor alone knows of the impossibility or illegally then existing or the promisor might have known as such after using reasonable diligence, such promisor is bound to compensate the promisee for any loss he may suffer through the non-performance of the promise inspite of the agreement being void *ab-initio* (Section 56, para 3).

In *Satyabarta Ghose v. Mugnuram A.I.R. 1954 S.C. 44* the Supreme Court interpreted the term 'impossible' appearing in second paragraph of Section 56. The Court observed that the word 'impossible' has not been used here in the sense of physical or literal impossibility. The performance of an act may not be literally impossible but it may be impracticable and useless from the point of view of the object and purpose which the parties had in view; and if an untoward event or change of circumstances totally upsets the very foundation upon which the parties rested their bargain; it can very well be said that the promisor found it impossible to do the act which he promised to do. In this case, A undertook to sell a plot of land to B but before the plot could be developed, war broke out and the land was temporarily requisitioned by the Government. A offered to return earnest money to B in cancellation of contract. B did not accept and sued A for specific performance. A pleaded discharge by frustration. The Court held that Section 56 is not applicable on the ground that the requisition was of temporary nature and there was no time limit within which A was obliged to perform the contract. The impossibility was not of such a nature which would strike at the root of the contract.

#### **Discharge by Supervening Impossibility**

A contract will be discharged by subsequent or supervening impossibility in any of the following ways:

- (a) Where the subject-matter of the contract is destroyed without the fault of the parties, the contract is discharged.
- (b) When a contract is entered into on the basis of the continued existence of a certain state of affairs, the contract is discharged if the state of things changes or ceases to exist.
- (c) Where the personal qualifications of a party is the basis of the contract, the contract is discharged by the death or physical disablement of that party.

### ***Discharge by Supervening Illegality***

A contract which is contrary to law at the time of its formation is void. But if, after the making of the contract, owing to alteration of the law or the act of some person armed with statutory authority the performance of the contract becomes impossible, the contract is discharged. This is so because the performance of the promise is prevented or prohibited by a subsequent change in the law. A enters into contract with B for cutting trees. By a statutory provision cutting of trees is prohibited except under a licence and the same is refused to A. The contract is discharged.

### **Cases in which there is no supervening impossibility**

In the following cases contracts are not discharged on the ground of supervening impossibility—

- (a) *Difficulty of performance*: The mere fact that performance is more difficult or expensive than the parties anticipated does not discharge the duty to perform.
- (b) *Commercial impossibilities* do not discharge the contract. A contract is not discharged merely because expectation of higher profits is not realised.
- (c) Strikes, lockouts and civil disturbance like riots do not terminate contracts unless there is a clause in the contract providing for non-performance in such cases.

Supervening impossibility or illegality is known as frustration under English Law.

### **(f) Discharge by Breach**

Where the promisor neither performs his contract nor does he tender performance, or where the performance is defective, there is a breach of contract. The breach of contract may be (i) actual; or (ii) anticipatory. The actual breach may take place either at the time the performance is due, or when actually performing the contract. Anticipatory breach means a breach before the time for the performance has arrived. This may also take place in two ways – by the promisor doing an act which makes the performance of his promise impossible or by the promisor in some other way showing his intention not to perform it.

### **Anticipatory Breach of Contract**

Breach of contract may occur, before the time for performance is due. This may happen where one of the parties definitely renounces the contract and shows his intention not to perform it or does some act which makes performance impossible. The other party, on such a breach being committed, has a right of action for damages.

He may either sue for breach of contract immediately after repudiation or wait till the actual date when performance is due and then sue for breach. If the promisee adopts the latter course, i.e., waits till the date when performance is due, he keeps the contract alive for the benefit of the promisor as well as for his own. He remains liable under it and enables the promisor not only to complete the contract in spite of previous repudiation, but also to avail himself of any excuse for non-performance which may have come into existence before the time fixed for performance.

In *Hochester v. De La Tour* (1853) E.R. 922, A hired B in April to act as a courier commencing employment from 1st June, but wrote to B in May repudiating the agreement, B sued A for breach of contract immediately after repudiation. A contended that there could not be breach of contract before June 1. *Held*, B was immediately entitled to sue and need not wait till 1st June, for his right of action to accrue.

In *Avery v. Bowden* (1856) 116 E.R. 1122, A hired B's ship to carry a cargo from Russia. Later on B repudiated the contract. A delayed taking action hoping B would change his mind before the performance

date. War broke out between Russia and Britain before the performance date frustrating the contract. *Held*, A lost his right to sue B for damages by his delay.

In *Frost v. Knight* (1872) L.R. 7 Ex. 111, the law on the subject of anticipatory breach was summed up as follows:

"The promisee if he pleases may treat the notice of intention as inoperative and await the time when the contract is to be executed and then hold the other party responsible for all the consequences of non-performance: but in that case he keeps the contract alive for the benefit of the other party as well as his own; he remains subject to all his own obligations and liabilities under it, and enables the other party not only to complete the contract, if so advised, notwithstanding his previous repudiation of it, but also to take advantage of any supervening circumstances which would justify him in declining to complete it. "

## REMEDIES FOR BREACH

Where a contract is broken, the injured party has several courses of action open to him. The appropriate remedy in any case will depend upon the subject-matter of the contract and the nature of the breach.

### (i) Remedies for Breach of Contract

In case of breach of contract, the injured party may:

- (a) Rescind the contract and refuse further performance of the contract;
- (b) Sue for damages;
- (c) Sue for specific performance;
- (d) Sue for an injunction to restrain the breach of a negative term; and
- (e) Sue on *quantum meruit*

When a party to a contract has broken the contract, the other party may treat the contract as rescinded and he is absolved from all his obligations under the contract. Under Section 65, when a party treats the contract as rescinded, he makes himself liable to restore any benefits he has received under the contract to the party from whom such benefits were received. Under Section 75 of the Indian Contract Act, if a person rightfully rescinds a contract, he is entitled to a compensation for any damage which he has sustained through the non-fulfilment of the contract by the other party. Section 64 deals with consequences of rescission of voidable contracts, i.e., where there is flaw in the consent of one party to the contract. Under this Section when a person at whose option a contract is voidable rescinds, the other party thereto need not perform any promise therein contained in which he is the promisor. The party rescinding a voidable contract shall, if he has received any benefit thereunder, from another party to such contract, restore such benefit so far as may be, to the person from whom it was received.

### (ii) Damages for Breach of Contract

Under Section 73 of the Indian Contract Act, when a contract has been broken, a party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage, caused to him thereby, *which naturally arose in the usual course of things from such breach or which the parties knew, when they made the contract to be likely to result from the breach of it*. Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

The foundation of the claim for damages rests in the celebrated case of *Hadley v. Baxendale*, (1854) 9 Ex. 341. The facts of this case were as follows:

There was a breakdown of a shaft in A's mill. He delivered the shaft to B, a common carrier to be taken to a

manufacturer to copy and make a new one. A did not make known to B that delay would result in loss of profits. By some neglect on the part of B, the *delivery of the shaft was delayed in transit beyond a reasonable time*. As a result, the mill was idle for a longer period than it would otherwise have been, had there been no such delay. It was held, B was not liable for the loss of profits during the period of delay as the circumstances communicated to A did not show that the delay in the delivery of the shaft would entail loss of profits to the mill. In the course of the judgement it was observed:

"Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties at the time they made the contract as the probable result of the breach of it. Now, if the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants and thus known to both the parties, the damages resulting from the breach of such a contract which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated. But, on other hand, if these special circumstances were wholly unknown to the party breaking the contract, he at the most could only be supposed to have had in his contemplation, the amount of injury which would arise generally and in the great multitude of cases not affected by any special circumstances from such breach of contract. For, had the special circumstances been known, the parties might have specially provided for the breach of contract by special terms as to damages in that case and of this advantage it would be very unjust to deprive them."

*Liquidated and Unliquidated damages:* Where the contracting parties agree in advance the amount payable in the event of breach, the sum payable is called *liquidated damages*.

Where the amount of compensation claimed for a breach of contract is left to be assessed by the Court, damages claimed are called *unliquidated damages*.

### Unliquidated Damages

Those are of the following kinds:

- (a) general or ordinary damages, (b) special damages (c) exemplary or punitive damages, and (d) nominal damages.

### Ordinary Damages

These are restricted to pecuniary compensation to put the injured party in the position he would have been had the contract been performed. It is the estimated amount of loss actually incurred. Thus, it applies only to the proximate consequences of the breach of the contract and the remote consequences are not generally regarded. For example, in a contract for the sale of goods, the damages payable would be the difference between the contract price and the price at which the goods are available on the date of the breach.

### Special Damages

Special damages are those resulting from a breach of contract under some peculiar circumstances. If at the time of entering into the contract, the party has notice of special circumstances which makes special loss the likely result of the breach in the ordinary course of things, then upon his-breaking the contract and the special loss following this breach, he will be required to make good the special loss. For example, A delivered goods to the Railway Administration to be carried to a place where an exhibition was being held and told the goods clerk that if the goods did not reach the destination on the stipulated date he would suffer a special loss. The goods reached late. He was entitled to claim special damages.

### **Exemplary Damages**

These damages are awarded to punish the defendant and are not, as a rule, granted in case of breach of contract. In two cases, however, the court may award such damages, viz.,

- (i) breach of promise to marry; and
- (ii) wrongful dishonour of a customers cheque by the banker.

In a breach of promise to marry, the amount of the damages will depend upon the extent of injury to the party's feelings. In the bankers case, the smaller the amount of the cheque dishonoured, larger will be damages as the credit of the customer would be injured in a far greater measure, if a cheque for a small amount is wrongfully dishonoured.

### **Nominal Damages**

Nominal damages consist of a small token award, e.g., a rupee or even 25 paise, where there has been an infringement of contractual rights, but no actual loss has been suffered. These damages are awarded to establish the right to decree for breach of contract.

### **Liquidated Damages and Penalty**

Where the contracting parties fix at the time of contract the amount of damages that would be payable in case of breach, in English law, the question may arise whether the term amounts to "liquidated damages" or a "penalty"? The Courts in England usually give effect to liquidated damages, but they always relieve against penalty.

The test of the two is that where the amount fixed is a genuine pre-estimate of the loss in case of breach, it is liquidated damages and will be allowed. If the amount fixed is without any regard to probable loss, but is intended to frighten the party and to prevent him from committing breach, it is a penalty and will not be allowed.

In Indian law, there is no such difference between liquidated damages and penalty. Section 74 provides for "reasonable compensation" upto the stipulated amount whether it is by way of liquidated damages or penalty. For example, A borrows Rs. 500 from B and promises to pay Rs. 1,000 if he fails to repay Rs. 500 on the stipulated date. On A's failure to repay on the given date, B is entitled to recover from A such compensation, not exceeding Rs. 1,000 as the Court may consider reasonable. (*Union of India v. Raman Iron Foundry*, AIR 1974 SC 1265).

### **(iii) Specific Performance**

It means the actual carrying out by the parties of their contract, and in proper cases the Court will insist upon the parties carrying out this agreement. Where a party fails to perform the contract, the Court may, at its discretion, order the defendant to carry out his undertaking according to the terms of the contract. A decree for specific performance may be granted in addition to or instead of damages.

Specific performance is usually granted in contracts connected with land, e.g., purchase of a particular plot or house, or to take debentures in a company. In case of sale of goods, it will only be granted if the goods are unique and cannot be purchased in the market, e.g., a particular race horse, or one of special value to the party suing by reason of personal or family association, e.g., an heirloom.

Specific performance will not be ordered:

- (a) where monetary compensation is an adequate remedy;

- (b) where the Court cannot supervise the execution of the contract, e.g., a building contract;
- (c) where the contract is for personal service; and
- (d) where one of the parties is a minor.

#### **(iv) Injunction**

An injunction, is an order of a Court restraining a person from doing a particular act. It is a mode of securing the specific performance of a negative term of the contract, (i.e., where he is doing something which he promises not to do), the Court may in its discretion issue an order to the defendant restraining him from doing what he promised not to do. Injunction may be prohibitory or mandatory. In prohibitory, the Court restrains the commission of a wrongful act whereas in mandatory, it restrains continuance of a wrongful commission.

In *Lumley v. Wagner* (1852) 90 R.R. 125. W agreed to sing at L's theatre and nowhere else. W, in breach of contract with L entered into a contract to sing for Z. *Held*, although W could not be compelled to sing at Ls theatre, yet she could be restrained by injunction from singing for Z.

### **CONTRACT OF INDEMNITY AND GUARANTEE (Sections 124 to 147)**

#### **Meaning of Indemnity**

A contract of indemnity is a contract by which one party promises to save the other party from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person (Section 124). For example, A contracts to indemnify B against the consequence of any proceedings which C may take against B in respect of a certain sum of 300 rupees. This is a contract of indemnity. The contract of indemnity may be express or implied. The later may be inferred from the circumstances of a particular case, e.g., an act done by A at the request of B. If A incurs any expenses, he can recover the same from B.

The person who promises to indemnify or make good the loss is called the indemnifier and the person whose loss is made good is called the indemnified or the indemnity holder. A contract of insurance is an example of a contract of indemnity according to English Law. In consideration of premium, the insurer promises to make good the loss suffered by the assured on account of the destruction by fire of his property insured against fire.

Under the Indian Contract Act, the contract of indemnity is restricted to such cases only where the loss promised to be reimbursed, is caused by the conduct of the promisor or of any other person. The loss caused by events or accidents which do not depend on the conduct of any person, it seems, cannot be sought to be reimbursed under a contract of indemnity.

#### **Rights of Indemnity Holder when Sued**

Under Section 125, the promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor—

- (1) all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies;
- (2) all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as if it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorised him to bring or defend the suit; and

- (3) all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorised him to compromise the suit.

### Meaning of Contract of Guarantee

A contract of guarantee is a contract to perform the promise, or discharge the liability of a third person in case of his default. The person who gives the guarantee is called the Surety, the person for whom the guarantee is given is called the Principal Debtor, and the person to whom the guarantee is given is called the Creditor (Section 126). A guarantee may be either oral or written, although in the English law, it must be in writing.

### Illustration

A advances a loan of Rs. 5,000 to B and C promises to A that if B does not repay the loan, C will do so. This is a contract of guarantee. Here B is the principal debtor, A is the creditor and C is the surety or guarantor.

Like a contract of indemnity, a guarantee must also satisfy all the essential elements of a valid contract. There is, however, a special feature with regard to consideration in a contract of guarantee. The consideration received by the principal debtor is sufficient for surety. Section 127 provides that anything done or any promise made for the benefit of the principal debtor may be a sufficient consideration to the surety for giving the guarantee.

### Illustration

- (i) B requests A to sell and deliver to him goods on credit. A agrees to do so, provided C will guarantee the payment of the price of the goods. C promises to guarantee the payment in consideration of A's promise to deliver the goods. This is sufficient consideration for C's promise.
- (ii) A sells and delivers goods to B. C afterwards requests A to forbear to sue B for the debt for a year, and promises that if he does so, C will pay for them in default of payment by B. A agrees to forbear as requested. This is sufficient consideration for C's promise.

### Distinction between Indemnity and Guarantee

A contract of indemnity differs from a contract of guarantee in the following ways:

- (a) In a contract of indemnity there are only two parties: the indemnifier and the indemnified. In a contract of guarantee, there are three parties; the surety, the principal debtor and the creditor.
- (b) In a contract of indemnity, the liability of the indemnifier is primary. In a contract of guarantee, the liability of the surety is secondary. The surety is liable only if the principal debtor makes a default, the primary liability being that of the principal debtor.
- (c) The indemnifier need not necessarily act at the request of the debtor; the surety gives guarantee only at the request of the principal debtor.
- (d) In the case of a guarantee, there is an existing debt or duty, the performance of which is guaranteed by the surety, whereas in the case of indemnity, the possibility of any loss happening is the only contingency against which the indemnifier undertakes to indemnify.
- (e) The surety, on payment of the debt when the principal debtor has failed to pay is entitled to proceed against the principal debtor in his own right, but the indemnifier cannot sue third-parties in his own name, unless there be assignment. He must sue in the name of the indemnified.

## Extent of Surety's Liability

The liability of the surety is co-extensive with that of the principal debtor unless the contract otherwise provides (Section 128). A creditor is not bound to proceed against the principal debtor. He can sue the surety without suing the principal debtor. As soon as the debtor has made default in payment of the debt, the surety is immediately liable. But until default, the creditor cannot call upon the surety to pay. In this sense, the nature of the surety's liability is secondary.

## Illustration

A guarantees to B the payment of a bill of exchange by C, the acceptor. The bill is dishonoured by C. A is liable not only for the amount of the bill but also for any interest and charges which may have become due on it.

Section 128 only explains the quantum of a surety's obligation when terms of the contract do not limit it. Conversely it doesn't follow that the surety can never be liable when the principal debtor cannot be held liable. Thus, a surety is not discharged from liability by the mere fact that the contract between the principal debtor and creditor was voidable at the option of the former, and was avoided by the former. Where the agreement between the principal debtor and creditor is void as for example in the case of minority of principal debtor, the surety is liable as a principal debtor; for in such cases the contract of the so-called surety is not collateral, but a principal contract (*Kashiba v. Shripat* (1894) 19 Bom. 697).

## Kinds of Guarantees

A contract of guarantee may be for an existing debt, or for a future debt. It may be a specific guarantee, or it may be a continuing guarantee. A specific guarantee is given for a single debt and comes to an end when the debt guaranteed has been paid.

A continuing guarantee is one which extends to a series of transactions (Section 129). The liability of surety in case of a continuing guarantee extends to all the transactions contemplated until the revocation of the guarantee. As for instance, S, in consideration that C will employ P in collecting the rents of C's Zamindari, promises C to be responsible to the amount of Rs. 5,000 for the due collection and payment by P of these rents. This is a continuing guarantee.

## Revocation of Continuing Guarantee

A continuing guarantee is revoked in the following circumstances:

- By notice of revocation by the surety* (Section 130): The notice operates to revoke the surety's liability as regards future transactions. He continues to be liable for transactions entered into prior to the notice (*Offord v. Davies* (1862) 6 L.T.S. 79).
- By the death of the surety*: The death of the surety operates, in the absence of contract (*Lloyds v. Harper* (188) 16 Ch. D. 290) as a revocation of a continuing guarantee, so far as regards future transactions (Section 131). But for all the transactions made before his death, the surety's estate will be liable.

## Rights of Surety

A surety has certain rights against the creditor, (Section 141) the principal debtor (Sections 140 and 145) and the co-securities (Sections 146 and 147). Those are—

- Surety's rights against the creditor*: Under Section 141 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 suretyship is entered into whether the surety knows of the existence of such security or not; and, if

the creditor losses or, without the consent of the surety parts with such security, the surety is discharged to the extent of the value of the security.

- (b) *Rights against the principal debtor:* After discharging the debt, the surety steps into the shoes of the creditor or is subrogated to all the rights of the creditor against the principal debtor. He can then sue the principal debtor for the amount paid by him to the creditor on the debtors default; he becomes a creditor of the principal debtor for what he has paid.

In some circumstances, the surety may get certain rights even before payment. The surety has remedies against the principal debtor before payment and after payment. In *Mamta Ghose v. United Industrial Bank* (AIR 1987 Cal. 180) where the principal debtor, after finding that the debt became due, started disposing of his properties to prevent seizure by surety, the Court granted an injunction to the surety restraining the principal debtor from doing so. The surety can compel the debtor, after debt has become due to exonerate him from his liability by paying the debt.

- (c) *Surety's rights gains co-sureties:* When a surety has paid more than his share of debt to the creditor, he has a right of contribution from the co-securities who are equally bound to pay with him. A, B and C are sureties to D for the sum of Rs. 3,000 lent to E who makes default in payment. A, B and C are liable, as between themselves to pay Rs. 1,000 each. If any one of them has to pay more than Rs. 1,000 he can claim contribution from the other two to reduce his payment to only Rs. 1,000. If one of them becomes insolvent, the other two shall have to contribute the unpaid amount equally.

## Discharge of Surety

A surety may be discharged from liability under the following circumstances:

- (a) By notice of revocation in case of a continuing guarantee as regards future transaction (Section 130.)
- (b) By the death of the surety as regards future transactions, in a continuing guarantee in the absence of a contract to the contrary (Section 131).
- (c) Any variation in the terms of the contract between the creditor and the principal debtor, without the consent of the surety, discharges the surety as regards all transactions taking place after the variation (Section 133).
- (d) A surety will be discharged if the creditor releases the principal debtor, or acts or makes an omission which results in the discharge of the principal debtor (Section 134). But where the creditor fails to sue the principal debtor within the limitation period, the surety is not discharged.
- (e) Where the creditor, without the consent of the surety, makes an arrangement with the principal debtor for composition, or promises to give time or not to sue him, the surety will be discharged (Section 135).
- (f) If the creditor does any act which is against the rights of the surety, or omits to do an act which his duty to the surety requires him to do, and the eventual remedy of the surety himself against the principal debtor is thereby impaired, the surety is discharged (Section 139).
- (g) If the creditor loses or parts with any security which at the time of the contract the debtor had given in favour of the creditor, the surety is discharged to the extent of the value of the security, unless the surety consented to the release of such security by creditor in favour of the debtor. It is immaterial whether the surety was or is aware of such security or not (Section 141).

## CONTRACT OF BAILMENT AND PLEDGE

### (a) Bailment

A bailment is a transaction whereby one person delivers goods to another person for some purpose, upon a

contract that they are, when the purpose is accomplished to be returned or otherwise disposed of according to the directions of the person delivering them (Section 148). The person who delivers the goods is called the *bailor* and the person to whom they are delivered is called the *bailee*.

Bailment is a *voluntary delivery of goods for a temporary purpose* on the understanding that *they are to be returned in specie* in the same or altered form. The ownership of the goods remains with the bailor, the bailee getting only the possession. Delivery of goods may be actual or constructive, e.g., where the key of a godown is handed over to another person, it amounts to delivery of goods in the godown.

### Gratuitous Bailment

A gratuitous bailment is one in which neither the bailor nor the bailee is entitled to any remuneration. Such a bailment may be for the exclusive benefit of the bailor, e.g., when A leaves his dog with a neighbour to be looked after in A's absence on a holiday. It may again be for exclusive benefit of the bailee, e.g., where you lend your book to a friend of yours for a week. In neither case any charge is made.

A gratuitous bailment terminates by the death of either the bailor or the bailee (Section 162).

Under Section 159 the lender of a thing for use may at any time require its return if the loan was gratuitous, even though he lent it for a specified time or purpose. But if on the faith of such loan made for a specified time or purpose, the borrower has acted in such a manner that the return of the thing lent before the time agreed upon would cause him loss exceeding the benefit actually derived by him from the loan, the lender must, if he compels the return, indemnify the borrower the amount in which the loss so occasioned exceeds the benefit so derived.

### Bailment for Reward

This is for the mutual benefit of both the bailor and the bailee. For example, A lets out a motor-car for hire to B. A is the bailor and receives the hire charges and B is the bailee and gets the use of the car. Where, A hands over his goods to B, a carrier for carriage at a price, A is the bailor who enjoys the benefit of carriage and B is the bailee who receives a remuneration for carrying the goods.

### Duties of Bailee

The bailee owes the following duties in respect of the goods bailed to him:

- The bailee must take as much care of the goods bailed to him as a man of ordinary prudence would take under similar circumstances of his own goods of the same bulk, quality and value as the goods bailed (Section 151). If he takes this much care he will not be liable for any loss, destruction or deterioration of the goods bailed (Section 152). The *degree of care required from the bailee is the same whether the bailment is for reward or gratuitous*.

Of course, the bailee may agree to take special care of the goods, e.g., he may agree to keep the property safe from all perils and answers for accidents or thefts. But even such a bailee will not be liable for loss happening by *an act of God* or by public enemies.

- The bailee is under a duty not to use the goods in an unauthorised manner or for unauthorised purpose (Section 153). If he does so, the bailor can terminate the bailment and claim damages for any loss or damage caused by the unauthorised use (Section 154).
- He must keep the goods bailed to him separate from his own goods (Sections 155-157).

If the bailee without the consent of the bailor, mixes the goods of the bailor with his own goods, the bailor and the bailee shall have an interest, in proportion to their respective shares, in the mixture

thus produced. If the bailee without the consent of the bailor, mixes the goods of the bailor with his own goods, and the goods can be separated or divided, the property in the goods remains in the parties respectively; but the bailee is bound to bear the expenses of separation, and any damages arising from the mixture.

If the bailee without the consent of the bailor mixes, the goods of the bailor with his own goods, in such a manner that it is impossible to separate the goods bailed from the other goods and deliver them back, the bailor is entitled to be compensated by the bailee for the loss of goods.

- (d) He must not set up an adverse title to the goods.
- (e) It is the duty of the bailee to return the goods without demand on the expiry of the time fixed or when the purpose is accomplished (Section 160). If he fails to return them, he shall be liable for any loss, destruction or deterioration of the goods even without negligence on his part (Section 161).
- (f) In the absence of any contract to the contrary, the bailee must return to the bailor any increase, or profits which may have accrued from the goods bailed; for example, when A leaves a cow in the custody of B to be taken care of and the cow gets a calf, B is bound to deliver the cow as well as the calf to A (Section 163).

### **Bailees Particular Lien (Section 170)**

Where the goods are bailed for a particular purpose and the bailee in due performance of bailment, expands his skill and labour, he has in the absence of an agreement to the contrary a lien on the goods, i.e., the bailee can retain the goods until his charges in respect of labour and skill used on the goods are paid by the bailor. A gives a piece of cloth to B, a tailor, for making it into a suit, B promises to have the suit ready for delivery within a fortnight, B has the suit ready for delivery. He has a right to retain the suit until he is paid his dues. The section expresses the Common Law principle that if a man has an article delivered to him on the improvement of which he has to bestow trouble and expenses, he has a right to detain it until his demand is paid.

The right of lien arises only where labour and skill have been used so as to confer an additional value on the article.

### **Particular and General Lien**

Lien is of two kinds: Particular lien and General lien. A particular lien is one which is available only against that property of which the skill and labour have been exercised. A bailee's lien is a particular lien.

A *general lien* is a right to detain any property belonging to the other and in the possession of the person trying to exercise the lien in respect of any payment lawfully due to him.

Thus, a general lien is the right to retain the property of another for a general balance of accounts but a particular lien is a right to retain only for a charge on account of labour employed or expenses bestowed upon the identical property detained.

The right of general lien is expressly given by Section 171 of the Indian Contract Act to bankers, factors, warfingers, attorneys of High Court and policy-brokers, provided there is no agreement to the contrary.

### **Duties of bailor**

The bailor has the following duties:

- (a) The bailor must disclose all the known faults in the goods; and if he fails to do that, he will be liable for any damage resulting directly from the faults (Section 150). For example, A delivers to B, a carrier, some explosive in a case, but does not warn B. The case is handled without extraordinary

care necessary for such articles and explodes. A is liable for all the resulting damage to men and other goods.

In the case of bailment for hire, a still greater responsibility is placed on the bailor. He will be liable even if he did not know of the defects (Section 150). A hires a carriage of B. The carriage is unsafe though B does not know this. A is injured. B is responsible to A for the injury.

- (b) It is the duty of the bailor to pay any extraordinary expenses incurred by the bailee. For example, if a horse is lent for a journey, the expense of feeding the horse would, of course, subject to any special agreement be borne by the bailee. If however the horse becomes ill and expenses have been incurred on its treatment, the bailor shall have to pay these expenses (Section 158).
- (c) The bailor is bound to indemnify the bailee for any cost or costs which the bailee may incur because of the defective title of the bailor of the goods bailed (Section 164).

### **Termination of bailment**

Where the bailee wrongfully uses or dispose of the goods bailed, the bailor may determine the bailment (Section 153.)

As soon as the period of bailment expires or the object of the bailment has been achieved, the bailment comes to an end, and the bailee must return the goods to the bailor (Section 160). Bailment is terminated when the subject matter of bailment is destroyed or by reason of change in its nature, becomes incapable of use for the purpose of bailment.

A gratuitous bailment can be terminated by the bailor at any time, even before the agreed time, subject to the limitation that where termination before the agreed period causes loss in excess of benefit, the bailor must compensate the bailee (Section 159).

A gratuitous bailment terminates by the death of either the bailor or the bailee (Section 162).

### **Finder of Lost Goods**

The position of a finder of lost goods is exactly that of a bailee. The rights of a finder are that he can sue the owner for any reward that might have been offered, and may retain the goods until he receives the reward. But where the owner has offered no reward, the finder has only a particular lien and can detain the goods until he receives compensation for the troubles and expenses incurred in preserving the property for finding out the true owner. But he cannot file a suit for the recovery of the compensation [Section 168].

Thus, as against the true owner, the finder of goods in a public or quasi public place is only a bailee; he keeps the article in trust for the real owner. As against every-one else, the property in the goods vests in the finder on his taking possession of it.

The finder has a right to sell the property—

- (a) where the owner cannot with reasonable diligence be found, or
- (b) when found, he refuses to pay the lawful charges of the finder and—
  - (i) if the thing is in danger of perishing or losing greater part of its value, or
  - (ii) when the lawful charges of the finder for the preservation of goods and the finding out of the owner amounts to two-thirds of the value of the thing (Section 169).

### **Carrier as Bailee**

A common carrier undertakes to carry goods of all persons who are willing to pay his usual or reasonable

rates. He further undertakes to carry them safely, and make good all losses, unless they are caused by act of God or public enemies. Carriers by land including railways and carriers by inland navigation, are common carriers. Carriers by Sea for hire are not common carriers and they can limit their liability. Railways in India are now common carriers.

*Inn-keepers:* The liability of a hotel keeper is governed by Sections 151 and 152 of the Contract Act and is that of an ordinary bailee with regard to the property of the guests.

C stayed in a room in a hotel. The hotel-keeper knew that the room was in an insecure condition. While C was dining in the dining room, some articles were stolen from his room. It was held that the hotel-keeper was liable as he should have taken reasonable steps to rectify the insecure condition of the rooms (*Jan & San v. Caneron* (1922) 44 All. 735).

### (b) Pledge

Pledge or pawn is a contract whereby an article is deposited with a lender of money or promisee as security for the repayment of a loan or performance of a *promise*. The bailor or depositor is called the Pawnor and the bailee or depositor the "Pawnee" (Section 172). Since pledge is a branch of bailment, the pawness is bound to take reasonable care of the goods pledged with him. Any kind of goods, valuables, documents or securities may be pledged. The Government securities, e.g., promissory notes must, however, be pledged by endorsement and delivery.

The following are the essential ingredients of a pledge:

- (i) The property pledged should be delivered to the pawnee.
- (ii) Delivery should be in pursuance of a contract.
- (iii) Delivery should be for the purpose of security.
- (iv) Delivery should be upon a condition to return.

### Rights of the Pawnee

No property in goods pawned passes to the pawnee, but the pawnee gets a "special property to retain possession even against the true owner until the payment of the debt, interest on the debt, and any other expense incurred in respect of the possession or for preservation of the goods pledged" (Section 173). The pawnee must return the goods to the pawnor on the tender of all that is due to him. The pawnee cannot confer a good title upon a *bona fide* purchaser for value.

Should the pawnor make a default in payment of the debt or performance of the promise at the stipulated time, the pawnee may-

- (i) file a suit for the recovery of the amount due to him while retaining the goods pledged as collateral security; or
- (ii) sue for the sale of the goods and the realisation of money due to him; or
- (iii) himself sell the goods pawned, after giving reasonable notice to the pawnor, sue for the deficiency, if any, after the sale.

If the sale is made in execution of a decree, the pawnee may buy the goods at the sale. But he cannot sell them to himself in a sale made by himself under (iii) above. If after sale of the goods, there is surplus, the pawnee must pay it to the pawnor (Section 176).

### Rights of Pawnor

On default by pawnor to repay on the stipulated date, the pawnee may sell the goods after giving reasonable

notice to the pawnor. If the pawnee makes an unauthorised sale without giving notice to the pawnor, the pawnor has the following rights—

- (i) He can file a suit for redemption of goods by depositing the money treating the sale as if it had never taken place; or
- (ii) He can ask for damages on the ground of conversion.

### Pledge by Non-owners

Ordinarily, the owner of the goods would pledge them to secure a loan but the law permits under certain circumstances a pledge by a person who is not the owner but is in possession of the goods. Thus, a valid pledge may be created by the following non-owners.

- (a) *A mercantile agent:* Where a mercantile agent is, with the consent of the owner, in possession of goods or the documents of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, is as valid as if he were expressly authorised by the owner of the goods to make the same. But the pledge is valid only if the pawnee acts in good faith and has not at the time of the pledge notice that the pawnor has not the authority to pledge (Section 178).
- (b) *Pledge by seller or buyer in possession after sale:* A seller, left in possession of goods sold, is no more the owner, but pledge by him will be valid, provided the pawnee acted in good faith and had no notice of the sale of goods to the buyer (Section 30 of The Sale of Goods Act 1930).
- (c) *Pledge where pawnor having limited interest:* When the pawnor is not the owner of the goods but has a limited interest in the goods which he pawns, e.g., he is a mortgagee or he has a lien with respect of these goods, the pledge will be valid to the extent of such interest.
- (d) *Pledge by co-owner in possession:* One of the several co-owners of goods in possession thereof with the assent of the other co-owners may create a valid pledge of the goods.
- (e) *Pledge by person in possession under a voidable contract:* A person may obtain possession under a contract which is voidable at the option of the lawful owner on the ground of misrepresentation, fraud, etc. The person in possession may pledge the goods before the contract is avoided by the other party (Section 178A).

## LAW OF AGENCY

### Definition of Agent (Section 182)

An agent is a person who is employed to bring his principal into contractual relations with third-parties. As the definition indicates, an agent is a mere connecting link between the principal and a third-party. But during the period that an agent is acting for his principal, he is clothed with the capacity of his principal.

### Creation of Agency

A contract of agency may be express or implied, (Section 186) but consideration is not an essential element in this contract (Section 185). Agency may also arise by estoppel, necessity or ratification.

- (a) *Express Agency:* A contract of agency may be made orally or in writing. The usual form of written contract of agency is the Power of Attorney, which gives him the authority to act on behalf of his principal in accordance with the terms and conditions therein. In an agency created to transfer immovable property, the power of attorney must be registered. A power of attorney may be general, giving several powers to the agent, or special, giving authority to the agent for transacting a single act.

- (b) *Implied Agency*: Implied agency may arise by conduct, situation of parties or necessity of the case.
- (i) *Agency by Estoppel* (Section 237): Estoppel arises when you are precluded from denying the truth of anything which you have represented as a fact, although it is not a fact. Thus, where P allows third-parties to believe that A is acting as his authorised agent, he will be estopped from denying the agency if such third-parties relying on it make a contract with A even when A had no authority at all.
  - (ii) *Wife as agent*: Where a husband and wife are living together, the wife is presumed to have her husband's authority to pledge his credit for the purchase of necessaries of life suitable to their standard of living. But the husband will not be liable if he shows that (i) he had expressly warned the trademan not to supply goods on credit to his wife; or (ii) he had expressly forbidden the wife to pledge his credit; or (iii) his wife was already sufficiently supplied with the articles in question; or (iv) she was supplied with a sufficient allowance.
- Similarly, where any person is held out by another as his agent, the third-party can hold that person liable for the acts of the ostensible agent, or the agent by holding out. Partners are each other's agents for making contracts in the ordinary course of the partnership business.
- (iii) *Agency of Necessity* (Sections 188 and 189): In certain circumstances, a person who has been entrusted with another's property, may have to incur unauthorised expenses to protect or preserve it. Such an agency is called an agency of necessity. For example, A sent a horse by railway and on its arrival at the destination there was no one to receive it. The railway company, being bound to take reasonable steps to keep the horse alive, was an agent of necessity of A.
- A wife deserted by her husband and thus forced to live separate from him, can pledge her husband's credit to buy all necessaries of life according to the position of the husband even against his wishes.
- (iv) *Agency by ratification* (Sections 169-200): Where a person having no authority purports to act as agent, or a duly appointed agent exceeds his authority, the principal is not bound by the contract supposedly based on his behalf. But the principal may ratify the agent's transaction and so accept liability. In this way an agency by ratification arises. This is also known as *ex post facto agency*—agency arising after the event. The effect of ratification is to render the contract binding on the principal as if the agent had been authorised before hand. Also ratification relates back to the original making of the contract so that the agency is taken to have come into existence from the moment the agent first acted, and not from the date the principal ratified it. Ratification is effective only if the following conditions are satisfied—
- (a) The agent must expressly contract as agent for a principal who is in existence and competent to contract.
  - (b) The principal must be competent to contract not only at the time the agent acted, but also when he ratified the agent's act.
  - (c) The principal at the time of ratification has full knowledge of the material facts, and must ratify the whole contract, within a reasonable time.
  - (d) Ratification cannot be made so as to subject a third-party to damages, or terminate any right or interest of a third person.
  - (e) Only lawful acts can be ratified.

### Classes of Agents

Agents may be special or general or, they may be mercantile agents:

- (a) *Special Agent*: A special agent is one who is appointed to do a specified act, or to perform a

specified function. He has no authority outside this special task. The third-party has no right to assume that the agent has unlimited authority. Any act of the agent beyond that authority will not bind the principal.

- (b) *General Agent*: A general agent is appointed to do anything within the authority given to him by the principal in all transactions, or in all transactions relating to a specified trade or matter. The third-party may assume that such an agent has power to do all that is usual for a general agent to do in the business involved. The third party is not affected by any private restrictions on the agents authority.

### Sub-Agent

A person who is appointed by the agent and to whom the principal's work is delegated to known as sub-agent. Section 191 provides that "a sub-agent is a person employed by, and acting under the control of the original agent in the business of the agency." So, the sub-agent is the agent of the original agent.

As between themselves, the relation of sub-agent and original agent is that of agent and the principal. A sub-agent is bound by all the duties of the original agent. The sub-agent is not directly responsible to the principal except for fraud and wilful wrong. The sub-agent is responsible to the original agent. The original agent is responsible to the principal for the acts of the sub-agent. As regards third persons, the principal is represented by sub-agent and he is bound and responsible for all the acts of sub-agent as if he were an agent originally appointed by the principal.

### Mercantile Agents

Section 2(9) of the Sale of Goods Act, 1930, defines a mercantile agent as "a mercantile agent having in the customary course of business as such agent authority either to sell goods or consign goods for the purposes of sale, or to buy goods, or to raise money on the security of goods". This definition covers factors, brokers, auctioneers, commission agents etc.

### Factors

A factor is a mercantile agent employed to sell goods which have been placed in his possession or contract to buy goods for his principal. He is the apparent owner of the goods in his custody and can sell them in his own name and receive payment for the goods. He has an insurable interest in the goods and also a general lien in respect of any claim he may have arising out of the agency.

### Brokers

A broker is a mercantile agent whose ordinary course of business is to make contracts with other parties for the sale and purchase of goods and securities of which he is not entrusted with the possession for a commission called brokerage. He acts in the name of principal. He has no lien over the goods as he is not in possession of them.

### *Del Credere* Agent

A *del credere* agent is a mercantile agent, who in consideration of an extra remuneration guarantees to his principal that the purchasers who buy on credit will pay for the goods they take. In the event of a third-party failing to pay, the *del credere* agent is bound to pay his principal the sum owned by third-party.

### Auctioneers

An auctioneer is an agent who sells goods by auction, i.e., to the highest bidder in public competition. He has

no authority to warrant his principal's title to the goods. He is an agent for the seller but after the goods have been knocked down he is agent for the buyer also for the purpose of evidence that the sale has taken place.

## Partners

In a partnership firm, every partner is an agent of the firm and of his co-partners for the purpose of the business of the firm.

## Bankers

The relationship between a banker and his customer is primarily that of debtor and creditor. In addition, a banker is an agent of his customer when he buys or sells securities, collects cheques, dividends, bills or promissory notes on behalf of his customer. He has a general lien on all securities and goods in his possession in respect of the general balance due to him by the customer.

## Duties of the Agent

An agent's duties towards his principal are as follows (which give corresponding rights to the principal who may sue for damages in the event of a breach of duty by the agent):

- (a) An agent must act within the scope of the authority conferred upon him and carry out strictly the instructions of the principal (Section 211).
- (b) in the absence of express instructions, he must follow the custom prevailing in the same kind of business at the place where the agent conducts the business (Section 211).
- (c) He must do the work with reasonable skill and diligence whereby the nature of his profession, the agent purports to have special skill, he must exercise the skill which is expected from the members of the profession (Section 212).
- (d) He must disclose promptly any material information coming to his knowledge which is likely to influence the principal in the making of the contract.
- (e) He must not disclose confidential information entrusted to him by his principal (Section 213).
- (f) He must not allow his interest to conflict with his duty, e.g., he must not compete with his principal (Section 215).
- (g) The agent must keep true accounts and must be prepared on reasonable notice to render an account.
- (h) He must not make any secret profit; he must disclose any extra profit that he may make.

Where an agent is discovered taking secret bribe, etc., the principal is entitled to (i) dismiss the agent without notice, (ii) recover the amount of secret profit, and (iii) refuse to pay the agent his remuneration. He may repudiate the contract, if the third-party is involved in secret profit and also recover damages.

- (i) An agent must not delegate his authority to sub-agent. A sub-agent is a person employed by and acting under the control of the original agent in the business of agency (Section 191). This rule is based on the principle: *Delegatus non-protest delegare*—a delegate cannot further delegate (Section 190).

But there are exceptions to this rule and the agent may delegate (i) where delegation is allowed by the principal, (ii) where the trade custom or usage sanctions delegation, (iii) where delegation is essential for proper performance, (iv) where an emergency renders it imperative, (v) where nature of the work is purely ministerial, and (vi) where the principal knows that the agent intends to delegate.

## Rights of Agents

Where the services rendered by the agent are not gratuitous or voluntary, the agent is entitled to receive the agreed remuneration, or if none was agreed, a reasonable remuneration. The agent becomes entitled to receive remuneration as soon as he has done what he had undertaken to do (Section 219).

Certain classes of agents, e.g., factors who have goods and property of their principal in their possession, have a lien on the goods or property in respect of their remuneration and expense and liabilities incurred. He has a right to stop the goods in transit where he is an unpaid seller.

As the agent represents the principal, the agent has a right to be indemnified by the principal against all charges, expenses and liabilities properly incurred by him in the course of the agency (Sections 222-223).

## Extent of Agent's Authority

The extent of the authority of an agent depends upon the terms expressed in his appointment or it may be implied by the circumstances of the case. The contractual authority is the real authority, but implied authority is to do whatever is incidental to carry out the real authority. This implied authority is also known as apparent or ostensible authority. Thus, an agent having an authority to do an act has authority to do everything lawful which is necessary for the purpose or usually done in the course of conducting business.

An agent has authority to do all such things which may be necessary to protect the principal from loss in an emergency and which he would do to protect his own property under similar circumstances. Where butter was becoming useless owing to delay in transit and was therefore sold by the station master for the best price available as it was not possible to obtain instructions from the principal, the sale was held binding upon the principal.

## Responsibilities of Principal to Third-parties

The effect of a contract made by an agent varies according to the circumstances under which the agent contracted. There are three circumstances in which an agent may contract, namely—

- (i) the agent acts for a named principal;
- (ii) the agent acts for an undisclosed principal; and
- (iii) the agent acts for a concealed principal.

(a) *Disclosed principal:* Where the agent contracts as agent for a named principal, he generally incurs neither rights nor liabilities under the contract, and drops out as soon as it is made. The contract is made between the principal and the third-party and it is between these two that rights and obligations are created. The legal effect is the same as if the principal had contracted directly with the third-party.

The effect is that the principal is bound by all acts of the agent done within the scope of actual, apparent or ostensible authority. This ostensible authority of the agent is important, for the acts of a general agent are binding on the principal if they are within the scope of his apparent authority, although they may be outside the scope of his actual authority. Therefore, a private or secret limitation or restriction of powers of an agent do not bind innocent third-party.

(b) *Undisclosed principal:* Where the agent discloses that he is merely an agent but conceals the identity of his principal, he is not personally liable, as he drops out in normal way. The principal, on being discovered, will be responsible for the contract made by the agent.

(c) *Concealed principal:* Where an agent appears to be contracting on his own behalf, without either

contracting as an agent or disclosing the existence of an agency (i.e., he discloses neither the name of the principal nor his existence), he becomes personally liable. The third-party may sue either the principal (when discovered) or the agent or both. If the third-party chooses to sue the principal and not the agent, he must allow the principal the benefit of all payments made by him to the agent on account of the contract before the agency was disclosed. The third-party is also entitled to get the benefit of anything he may have paid to the agent.

If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfil the contract if he can show that, if he had known who was the principal in the contract, or if he had known that the agent was not the principal, he would not have entered into the contract.

### **Principal Liable for Agent's Torts (Section 238)**

If an agent commits a tort or other wrong (e.g., misrepresentation or fraud) during his agency, whilst acting within the scope of his actual or apparent authority, the principal is liable. But the agent is also personally liable, and he may be sued also. The principal is liable even if the tort is committed exclusively for the benefit of the agent and against the interests of the principal.

### **Personal Liability of Agent to Third-party**

An agent is personally liable in the following cases:

- (a) Where the agent has agreed to be personally liable to the third-party.
- (b) Where an agent acts for a principal residing abroad.
- (c) When the agent signs a negotiable instrument in his own name without making it clear that he is signing it only as agent.
- (d) When an agent acts for a principal who cannot be sued (e.g., he is minor), the agent is personally liable.
- (e) An agent is liable for breach of warranty of authority. Where a person contracts as agent without any authority there is a breach of warranty of authority. He is liable to the person who has relied on the warranty of authority and has suffered loss.
- (f) Where authority is one coupled with interest or where trade, usage or custom makes the agent personally liable, he will be liable to the third-party.
- (g) He is also liable for his torts committed in the course of agency.

### **Meaning of Authority Coupled with Interest (Section 202)**

An agency is coupled with an interest when the agent has an interest in the authority granted to him or when the agent has an interest in the subject matter with which he is authorised to deal. Where the agent was appointed to enable him to secure some benefit already owed to him by the principal, the agency was coupled with an interest. For example, where a factor had made advances to the principal and is authorised to sell at the best price and recoup the advances made by him or where the agent is authorised to collect money from third-parties and pay himself the debt due by the principal, the agencies are coupled with interest. But a mere arrangement that the agent's remuneration is paid out of the rents collected by him, it does not give him any interest in the property and the agency is not the one coupled with an interest. An agency coupled with interest cannot be terminated in the absence of a contract to the contrary to the prejudice of such interest.

The principal laid down in Section 202 applies only if the following conditions are fulfilled:

- (i) The interest of the agent should exist at the time of creation of agency and should not have arisen

after the creation of agency.

- (ii) Authority given to the agent must be intended for the protection of the interest of the agent.
- (iii) The interest of the agent in the subject matter must be substantial and not ordinary.
- (iv) The interest of the agent should be over and above his remuneration. Mere prospect of remuneration is not sufficient interest.

### Termination of Agency

An agency comes to an end or terminates—

- (a) By the performance of the contract of agency; (Section 201)
- (b) By an agreement between the principal and the agent;
- (c) By expiration of the period fixed for the contract of agency;
- (d) By the death of the principal or the agency; (Section 201)
- (e) By the insanity of either the principal or the agent; (Section 201)
- (f) By the insolvency of the principal, and in some cases that of the agent; (Section 201)
- (g) Where the principal or agent is an incorporated company, by its dissolution;
- (h) By the destruction of the subject-matter; (Section 56)
- (i) By the renunciation of his authority by the agent; (Section 201)
- (j) By the revocation of authority by the principal. (Section 201)

### When Agency is Irrevocable

Revocation of an agency by the principal is not possible in the following cases:

- (a) Where the authority of agency is one coupled with an interest, even the death or insanity of the principal does not terminate the authority in this case (Section 202).
- (b) When agent has incurred personal liability, the agency becomes irrevocable.
- (c) When the authority has been partly exercised by the agent, it is irrevocable in particular with regard to obligations which arise from acts already done (Section 204).

### When Termination Takes Effect

Termination of an agency takes effect or is complete, as regards the agent when it becomes known to the agent. If the principal revokes the agent's authority, the revocation will take effect when the agent comes to know of it. As regards the third-parties, the termination takes effect when it comes to their knowledge (Section 208). Thus, if an agent whose authority has been terminated to his knowledge, enters into a contract with a third-party who deals with him *bona fide*, the contract will be binding on the principal as against the third-party. The termination of an agent's authority terminates the authority of the sub-agent appointed by the agent (Section 210).

The revocation of agency as regards the agent and as regards the principal takes effect at different points of time. Section 209 charges the agent with duty to protect the principal's interest where the principal dies or becomes of unsound mind. It provides that when an agency is terminated by the principal dying or becoming of unsound mind, the agent is bound to take, on behalf of the representatives of his late principal, all reasonable steps for the protection and preservation of the interest entrusted to him. So it is the duty of the agent to take all steps to protect the interest of his deceased principal on his death.

## JOINT VENTURE/ FOREIGN COLLABORATION/MULTINATIONAL AGREEMENTS

International business professionals use the term “modes of entry” to describe the different methods and approaches available to enter markets and conduct business in other countries. One mode of entry is the joint venture where two or more organizations join together in a cooperative effort to further their business goals. The joint venture is one of the most common and effective means of conducting business internationally. The joint venture documents and agreements are critical to the success of the venture. The joint venture agreement forms the basis of the understanding between and among the parties. It is relied upon to ensure that all parties understand their roles, rights, responsibilities, and remedies in the conduct of the venture. Organizations enter into joint ventures in good faith but closely scrutinize the joint venture documents if anything goes awry.

The importance of the documents and the purpose of this part is to cover, step by step, the critical elements to consider and include in joint venture agreements. Equity participation, for example, may or may not be as important as operational control. Technical participation in the venture may or may not be as important as the intellectual property rights that may result from the venture. A key to developing joint venture agreements is to determine goals and objectives in advance and ensure that the interests are reflected in the agreement.

Selection of a good local partner is the key to the success of any joint venture. Personal interviews with a prospective joint venture partner should be supplemented with proper due diligence. Once a partner is selected generally the parties highlighting the basis of the future joint venture agreement sign a memorandum of understanding or a letter of intent. Before signing the joint venture agreement, the terms should be thoroughly discussed to avoid any misunderstanding at a later stage. Negotiations require an understanding of the cultural and legal background of the parties.

It is difficult to prepare a set frame of the terms and conditions. The conditions may differ according to the requirements. While drafting a foreign collaboration agreement, the following factors should be kept in mind:

- Capability of the collaborator and the requirements of the party are clearly indicated.
- Clear definitions of technical terms are given.
- Specify if the product shall be manufactured/sold on exclusive or non-exclusive basis.
- Terms and conditions regarding nature of technical know-how, disclosure of drawings, specifications and other documents, furnishing of technical information in respect of processes with flow charts etc., plant outlay list of equipment, machinery and tool with specification have to be provided.
- Provisions for making available the engineers and/or skilled workers of the collaborator on payment of expenses relating to their stay per diem etc. are given.
- Details regarding specification and quality of the product to be manufactured are given.
- Quality control and trademarks to be used are also specified.
- Responsibility of the collaborator in establishing or maintaining assembly plants should be clearly determined and provided for.
- If sub-contracting of the work is involved, clarify if there would be any restrictions.
- The rate of royalty, mode of calculation and payment etc. Also, make provision as to who will bear the taxes/cess on such payments.
- Use of information and industrial property rights should also be provided for in the agreement.

- A clause on force majeure should be included.
- A clause that the collaborating company has to train the personnel of Indian company within a specified period should be incorporated. The clause should also specify the terms and conditions of such assistance, place of training, period of training and fees payable.
- A comprehensive clause on arbitration containing a clear provision as to the kind of arbitrator and place of arbitration should be included.
- There should be provision in the agreement for payment of interest on delayed payments.

## E-CONTRACT

Electronic contracts are not paper based but rather in electronic form are born out of the need for speed, convenience and efficiency. In the electronic age, the whole transaction can be completed in seconds, with both parties simply affixing their digital signatures to an electronic copy of the contract. There was initially an apprehension amongst the legislatures to recognize this modern technology, but now many countries have enacted laws to recognize electronic contracts. The conventional law relating to contracts is not sufficient to address all the issues that arise in electronic contracts. The Information Technology Act, 2000 solves some of the peculiar issues that arise in the formation and authentication of electronic contracts.

As in every other contract, an electronic contract also requires the following necessary ingredients:

- An offer needs to be made
- The offer needs to be accepted
- There has to be lawful consideration
- There has to be an intention to create legal relations
- The parties must be competent to contract
- There must be free and genuine consent
- The object of the contract must be lawful
- There must be certainty and possibility of performance.

## LESSON ROUND UP

- A contract is an agreement enforceable at law, made between two or more persons, by which rights are acquired by one or more to acts or forbearances on the part of the other or others.
- Every promise and every set of promises, forming the consideration for each other, is an agreement.
- All agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void.
- In flaw contract There may be the circumstances under which a contract made under these rules may still be bad, because there is a flaw, vice or error somewhere. As a result of such a flaw, the apparent agreement is not a real agreement.
- Section 27 of the Indian Contract Act states that every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is, to that extent, void.
- The literal meaning of the word "wager" is a "bet". Wagerning agreements are nothing but ordinary betting agreements.
- An agreement not enforceable by law is void *ab initio*.

- A contingent contract is a contract to do or not to do something, if some event *collateral to such contract*, does or does not happen. Contract of insurance and contracts of indemnity and guarantee are popular instances of contingent contracts.
- A quasi-contract rests on the equitable principle that a person shall not be allowed to enrich himself unjustly at the expense of another. In truth, it is not a contract at all. It is an obligation which the law creates, in the absence of any agreement, when any person is in the possession of one persons money, or its equivalent, under such circumstances that in equity and good conscience he ought not to retain it, and which in justice and fairness belongs to another. It is the duty and not an agreement or intention which defines it.
- A contract is said to be discharged or terminated when the rights and obligations arising out of a contract are extinguished.
- Where a contract is broken, the injured party has several courses of action open to him. The appropriate remedy in any case will depend upon the subject-matter of the contract and the nature of the breach.
- A contract of indemnity is a contract by which one party promises to save the other party from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person.
- A bailment is a transaction whereby one person delivers goods to another person for some purpose, upon a contract that they are, when the purpose is accomplished to be returned or otherwise disposed of according to the directions of the person delivering them.
- A contract of agency may be express or implied, but consideration is not an essential element in this contract. Agency may also arise by estoppel, necessity or ratification.

### SELF TEST QUESTIONS

1. Define consideration and state its essential features.
2. “No consideration, no contract”. Do you agree?
3. “The essence of every agreement is that there ought be free consent on both the sides”. Discuss.
4. How does a binding contract differ from other agreements?
5. Write short notes on:
  - (a) Reciprocal promises.
  - (b) “The law does not compel the impossible”.
  - (c) Substituted Agent.
  - (d) Liquidated Damages.

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# Lesson 9

## PREVENTION OF MONEY LAUNDERING

### LESSON OUTLINE

- Concept of money laundering
- Money laundering process
- Impact of money laundering on economic development
- Global initiatives for prevention of money laundering
- FAFT Recommendation
- Overview of Prevention of Money Laundering Act, 2002
- Adjudication and Adjudicating Authority
- Obligation of Banking Companies, Financial Institutions and Intermediary
- Summon, searches, seizures etc
- Retention of Property
- Retention of Record
- Appellate Tribunal
- Special Court
- KYC Guidelines
- KYC Policy
- Power of Central Government
- Agreement with foreign countries
- Attachment of property

### LEARNING OBJECTIVES

The globalization process, driven by advancements in communications and information technology, have made the international system more interactive, integrated, interrelated, and interconnected. This dynamic has unleashed the floodgates of opportunities for criminals to expand, widen and deepen their reach, become more sophisticated in their operations, and intensify their level and pace of transactions.

Because of the opportunities and needs created by the global dimension of business, crimes such as fraud, counterfeiting, corruption and embezzlement have opportunities to shift from individual or family ambit to more organized and competitive global structures.

The problem of money-laundering is no longer restricted to the geo political boundaries of any country. It is a global menace that cannot be contained by any nation alone. In view of this, India has become a member of the Financial Action Task Force and Asia Pacific Group on money-laundering, which are committed to the effective implementation and enforcement of internationally accepted standards against money-laundering and the financing of terrorism.

The Prevention of Money-laundering Act, 2002 addresses the international obligations under the Political Declaration and Global Programme of Action adopted by the General Assembly of the United Nations to prevent money laundering. The Act was amended in the year 2005, 2009 and 2012 to remove the difficulties arisen in implementation of the Act. Therefore, it is essential for the students to be familiar with the law relating to Prevention of Money-laundering Act, 2002.

The Prevention of Money-laundering Act, 2002 enacted to prevent money laundering and to provide for confiscation of property derived from, or involved in, money laundering and for matters connected therewith or incidental thereto.

## INTRODUCTION

Money laundering is the processing of criminal proceeds to disguise its illegal origin. Terrorism, illegal arms sales, financial crimes, smuggling, and the activities of organised crime, including drug trafficking and prostitution rings, generate huge sums. Embezzlement, insider trading, bribery and computer fraud also produce large profits and create an incentive to legitimise the ill-gotten gains through money laundering. When a criminal activity generates substantial profits, the individual or group involved in such activities route the funds to safe heavens by disguising the sources, changing the form, or moving the funds to a place where they are less likely to attract attention.

Most fundamentally, money laundering is inextricably linked to the underlying criminal activity that generates it. In essence, the laundering enables criminal activity to continue.

## Process of Money Laundering

The process of money laundering can be classified into three stages, namely, placement, layering and integration.

In the initial or placement stage of money laundering, the launderer introduces his illegal profits into the financial system, by breaking up large amounts of cash into less conspicuous smaller sums that are then deposited directly into a bank account, or by purchasing a series of monetary instruments that are later collected and deposited into accounts at another location.

After the funds are entered into the financial system, the layering takes place. In this stage, the launderer engages in a series of conversions or movements of the funds to distance them from their source. The funds might be channeled through the purchase and sale of investment instruments, or the launderer might simply wire the funds through a series of accounts at various banks across the globe.

After successful processing of criminal profits through the first two phases of the money laundering process, the launderer moves them to integration. In this stage the funds re-enter the legitimate economy. The launderer might choose to invest the funds into real estate, luxury assets, or business ventures.

## Impact of Money Laundering on Development

Economies with growing or developing financial centers, but inadequate controls are particularly vulnerable to money laundering, as against the established financial center countries, which implement comprehensive anti-money laundering regimes. The gaps in a national anti-money laundering system are exploited by launderers, who tend to move their networks to countries and financial systems with weak or ineffective countermeasures. As with the damaged integrity of an individual financial institution, there is a damping effect on foreign direct investment when a country's commercial and financial sectors are perceived to be subject to the control and influence of organised crime.

In times of decelerating growth, an infusion of hard currency can bolster a country's foreign reserves; ease the hardship associated with budget tightening policies and moderate foreign indebtedness. While these are short-term benefits associated with an inflow of criminal monies, the long-term effects are mostly negative. One difference between official borrowing and laundered funds is that the former can be controlled by Government, whereas the funds owned by criminals escape the governments ability to control and regulate the economy.

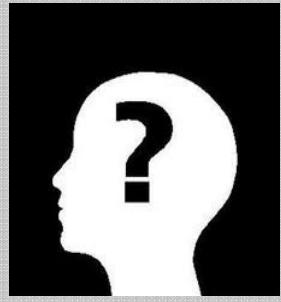
The possible social, economic and political effects of money laundering, if left unchecked or dealt with ineffectively, are serious. Through the process of money laundering, organised crime can infiltrate financial

institutions, acquire control of large sectors of the economy through investment, or offer bribes to public officials and indeed governments. Thus, the economic and political influence of criminal organisations can weaken the social fabric, ethical standards and ultimately the democratic institutions of society.

#### **What is the connection of money laundering with society at large?**

*The possible social and political costs of money laundering, if left unchecked or dealt with ineffectively, are serious. Organised crime can infiltrate financial institutions, acquire control of large sectors of the economy through investment, or offer bribes to public officials and indeed governments.*

*The economic and political influence of criminal organisations can weaken the social fabric, collective ethical standards, and ultimately the democratic institutions of society. In countries transitioning to democratic systems, this criminal influence can undermine the transition. Most fundamentally, money laundering is inextricably linked to the underlying criminal activity that generated it. Laundering enables criminal activity to continue.*



### **Prevention of Money Laundering – Global Initiatives**

Since money laundering is an international phenomenon, transnational co-operation is of critical importance in the fight against this menace. A number of initiatives have been taken to deal with the problem at international level. In this context, the United Nations or the Bank for International Settlements, took some initiatives in 1980s to address the problem of money laundering. However, with the creation of the Financial Action Task Force (FATF) in 1989, regional groupings, such as the European Union, Council of Europe, and organisation of American States also established anti- money laundering standards for their member countries.

The major international agreements addressing money laundering include the United Nations Convention against Illicit Trafficking in Drugs and Psychotropic Substances (the Vienna Convention) and Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime. The role of financial institutions in preventing and detecting money laundering has also been the subject of pronouncements by the Basle Committee on Banking Regulation Supervisory Practices, the European Union and the International Organization of Securities Commissions.

#### **The Vienna Convention**

The first major initiative in the prevention of money laundering was the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances in December 1988 (popularly known as Vienna Convention). This convention laid the groundwork for efforts to combat money laundering by obliging the member states to criminalize the laundering of money from drug trafficking. It promotes international cooperation in investigations and makes extradition between member states applicable to money laundering. The convention also establishes the principle that domestic bank secrecy provisions should not interfere with international criminal investigations.

#### **Council of Europe Convention**

The Council of Europe Convention on Laundering, Search, Seizure and Confiscation of Proceeds of Crime, 1990 establishes a common policy on money laundering. It sets out a common definition of money laundering and common measures for dealing with it. The Convention lays down the principles for

international cooperation among the member states, which may also include states outside the Council of Europe. This convention came into force in September 1993. One of the purposes of the convention is to facilitate international cooperation as regards investigative assistance, search, seizure and confiscation of the proceeds of all types of criminality, particularly serious crimes, such as, drug offences, arms dealing, terrorist offences etc. and other offences which generate large profits.

### **European Union Money Laundering Directive**

In response to the new opportunities for money laundering opened up by the liberalization of capital movements and cross-border financial services in the European Union, the Council of the European Communities in June, 1991 issued a directive on the Prevention of Use of the Financial System for the Purpose of Money Laundering. The directive requires member states to outlaw money laundering. The member states have been put under obligation to require financial institutions to establish and maintain internal systems to prevent laundering, to obtain the identification of customers with whom they enter into transaction of more than a particular amount and to keep proper records for at least five years. The financial institutions are also required to report suspicious transactions and ensure that such reporting does not result in liability for the institution or its employees.

### **Basle Committee's Statement of Principles**

In December 1988 the Basle Committee on Banking Regulation Supervisory Practices issued a statement of principles to be complied by the international banks of member states. These principles include identifying customers, avoiding suspicious transactions, and cooperating with law enforcement agencies. The statement aims at encouraging the banking sector to adopt common position in order to ensure that banks are not used to hide or launder funds acquired through criminal activities.

### **Resolution of the International Organization of Securities Commissions**

The International Organization of Securities Commissions (IOSCO) adopted, in October 1992, a resolution encouraging its members to take necessary steps to combat money laundering in securities and futures markets.

### **The Financial Action Task Force (FATF)**

The Financial Action Task Force (FATF) is an inter-governmental body established in 1989 by the Ministers of its Member jurisdictions. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The FATF is therefore a "policy-making body" which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas.

The FATF has developed a series of Recommendations that are recognised as the international standard for combating of money laundering and the financing of terrorism and proliferation of weapons of mass destruction. They form the basis for a co-ordinated response to these threats to the integrity of the financial system and help ensure a level playing field. First issued in 1990, the FATF Recommendations were revised in 1996, 2001, 2003 and in 2012 to ensure that they remain up to date and relevant, and they are intended to be of universal application.

The FATF monitors the progress of its members in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally. In collaboration with other international stakeholders, the

FATF works to identify national-level vulnerabilities with the aim of protecting the international financial system from misuse.

### History of the FATF

In response to mounting concern over money laundering, the Financial Action Task Force on Money Laundering (FATF) was established by the G-7 Summit that was held in Paris in 1989. Recognising the threat posed to the banking system and to financial institutions, the G-7 Heads of State or Government and President of the European Commission convened the Task Force from the G-7 member States, the European Commission and eight other countries.

### FATF Recommendations

The Task Force was given the responsibility of examining money laundering techniques and trends, reviewing the action which had already been taken at a national or international level, and setting out the measures that still needed to be taken to combat money laundering. In April 1990, less than one year after its creation, the FATF issued a report containing a set of Forty Recommendations, which were intended to provide a comprehensive plan of action needed to fight against money laundering.

In 2001, the development of standards in the fight against terrorist financing was added to the mission of the FATF. In October 2001 the FATF issued the *Eight Special Recommendations* to deal with the issue of terrorist financing. The continued evolution of money laundering techniques led the FATF to revise the FATF standards comprehensively in June 2003. In October 2004 the FATF published a Ninth Special Recommendations, further strengthening the agreed international standards for combating money laundering and terrorist financing - the *40+9 Recommendations*.

In February 2012, the FATF completed a thorough review of its standards and published the revised FATF Recommendations,. This revision is intended to strengthen global safeguards and further protect the integrity of the financial system by providing governments with stronger tools to take action against financial crime. They have been expanded to deal with new threats such as the financing of proliferation of weapons of mass destruction, and to be clearer on transparency and tougher on corruption. The 9 Special Recommendations on terrorist financing have been fully integrated with the measures against money laundering. This has resulted in a stronger and clearer set of standards.

### United Nations Global Programme Against Money Laundering

Office of the Drug Control and Crime Prevention implement this programme against Money Laundering with a view to increase the effectiveness of international action against money laundering through comprehensive technical cooperation services offered to Governments. The programme encompasses following three areas of activities, providing various means to states and institutions in their efforts to effectively combat money laundering:

- (i) Technical cooperation is the main task of the Programme. It encompasses activities of creating awareness, institution building and training.
- (ii) The research and analysis aims at offering States Key Information to better understand the phenomenon of money laundering and to enable the international community to devise more efficient and effective countermeasure strategies.
- (iii) The commitment to support the establishment of financial investigation services for raising the overall effectiveness of law enforcement measures.

The implementation of the Global Programme against Money Laundering is carried out in the spirit of cooperation with other international, regional and national organizations and institutions.

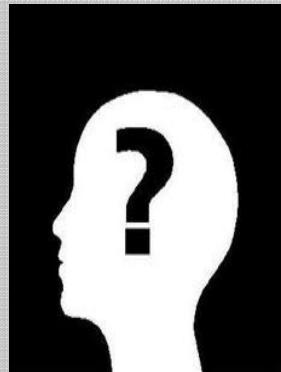
### ***What influence does money laundering have on economic development?***

*Launderers are continuously looking for new routes for laundering their funds. Economies with growing or developing financial centres, but inadequate controls are particularly vulnerable as established financial centre countries implement comprehensive anti-money laundering regimes.*

*Differences between national anti-money laundering systems will be exploited by launderers, who tend to move their networks to countries and financial systems with weak or ineffective countermeasures.*

*Some might argue that developing economies cannot afford to be too selective about the sources of capital they attract. But postponing action is dangerous. The more it is deferred, the more entrenched organised crime can become.*

*As with the damaged integrity of an individual financial institution, there is a damping effect on foreign direct investment when a country's commercial and financial sectors are perceived to be subject to the control and influence of organised crime. Fighting money laundering and terrorist financing is therefore a part of creating a business friendly environment which is a precondition for lasting economic development.*



### **Prevention of Money Laundering – Indian Initiatives**

In view of an urgent need for the enactment of a comprehensive legislation for preventing money-laundering and connected activities, confiscation of proceeds of crime, setting up of agencies and mechanisms for coordinating measures for combating money laundering etc., the Prevention of Money-Laundering Bill 1998 was introduced in the Parliament on the 4th August, 1998. The Bill was referred to the Standing Committee on Finance, which presented its report on the 4th March, 1999 to Lok Sabha. After incorporating the recommendations of the Standing Committee, the Government introduced the Prevention of Money Laundering Bill 1999 in the Parliament on October 29, 1999. The Bill received the assent of the President and became Prevention of Money Laundering Act, 2002 on 17th January 2003. The Act has come in force with effect from July 1, 2005. The Act was last amended in the year 2009, 2012.

### **Prevention of Money Laundering Act, 2002**

#### **Scheme of the Act**

The Prevention of Money Laundering Act, 2002 consists of ten chapters containing 75 sections and one Schedule divided into five parts. Chapter I containing section 1 and 2 deals with short title, extent and commencement and definitions. Chapter II containing sections 3 and 4 provides for offences and punishment for money laundering. Chapter III (Section 5-11) provides for attachment, adjudication and confiscation and Chapter IV (Sections 12-15) deals with obligations of banking companies, financial institutions and intermediaries. Chapter V (Sections 16-24) relates to Summons, Searches and Seizures etc.

The Act provides for establishment of Appellate Tribunal and thus sections 25-42 under Chapter VI provides for composition, procedure, power, jurisdiction etc. of the Appellate Tribunal. Chapter VII (Sections 43-47) deals with Special Courts, and Chapter VIII (Sections 48-54) provides for various authorities under the Act,

their appointment, powers, jurisdiction etc. Chapter IX (Sections 55-61) deals with reciprocal arrangement for assistance in certain matters and procedure for attachment and confiscation of property. Chapter X containing Sections 62-75 deals with miscellaneous provisions including punishment for, vexatious search, false information etc., cognizance of offences, and offences by companies, among others.

## Major Provisions of the Act

### Definitions

Section 2 of the Act defines various terms used in the Act. Some of the important definitions are given below:

### Attachment

Sub-section 1(d) defines attachment as to mean prohibition of transfer, conversion, disposition or movement of property by an order issued under Chapter III.

### Proceeds of Crime

Section 2(1)(u) defines the term 'proceeds of crime' as to mean any property derived or obtained, directly or indirectly by any person as a result of criminal activity relating to a scheduled offence or the value of any such property.

### Property

The term 'property' used in sub-section 1(v) of Section 2 means any property or assets of every description, whether, corporeal or incorporeal, movable or immovable, tangible or intangible and includes, deeds and instruments evidencing title to, or interest in such property or assets wherever located.

### Intermediary

The term intermediary under sub-section 1(n) of Section 2 has been defined as to mean a stock broker, sub-broker, share transfer agent, banker to an issue, trustee to a trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment advisor, and any other intermediary associated with securities market and registered under Section 12 of the SEBI Act, 1992.

### Investigation

Sub-section 2(1)(na) defines investigation to include all the proceedings under the Act conducted by the Director or by an authority authorized by the Central Government under this Act for the collection of evidence.

### Money Laundering

Section 3 of the Act states that whosoever directly or indirectly attempts to indulge or knowingly assists or knowingly is a party or actually involved in any process or activity connected with the proceeds of crime including its concealment, possession, acquisition or use and projecting or claiming it is an untainted property shall be guilty of offence of money laundering.

Section 4 provides that any person who 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 also liable to fine. However, where the proceeds of crime involved in money laundering relates to any offence specified under the Narcotic Drugs and Psychotropic Substances Act, the punishment may extend to rigorous imprisonment for ten years.

### **Attachment of property involved in money laundering**

Where the Director or any officer not below the rank of Deputy Director authorised by him, has reason to believe on the basis of material in his possession that any person is in possession of any proceeds of money laundering; such person has been charged of having committed a scheduled offence and such proceeds of crime are likely to be concealed, transferred or dealt with in any manner which may result in frustrating any proceedings relating to confiscation of such proceeds of crime, such officer may by order in writing, provisionally attach such property for a period not exceeding 180 days from the date of the order, in the manner provided in the Second Schedule of the Income-tax Act, 1961.

Every order of attachment shall cease to have effect after the expiry of ninety days from the date of the order or on the date of the order made by the Administrating Officer finding the person interested is not prevented from the enjoyment of property attached. 'Person interested in relation to any immovable property includes all persons claiming or entitled to claim any interest in the property. The Director or any other officer who provisionally attaches any property shall, within a period of 30 days from such attachment file a complaint, stating the facts of such attachment before the Adjudicating Authority.

### **Adjudicating Authority**

Section 6 empowers the Central Government to appoint, by notification, one or more persons not below the rank of Joint Secretary to the Government of India as Adjudicating Authority to exercise the jurisdiction, powers and authority conferred on or under the Act.

### **Adjudication**

Section 8 dealing with the adjudication provides that on receipt of a complaint from the Director or any other officer who provisionally attaches any property or an application made by such officer for retention of seized record or property, the Adjudicating Authority may, on reason to believe that any person has committed an offence of money laundering, serve a notice of not less than thirty days on such person calling upon him to indicate the sources of his income, earning or assets, out of which or by means of which he has acquired the property attached or seized, the evidence on which he relies and other relevant information and particulars and show cause why all or any of such property should not be declared to be the properties involved in money laundering and confiscated by the Central Government. Where a notice specifies any property as being held by a person on behalf of any other person, a copy of such notice shall also be served upon such other person. Similar notice is required to be served on all persons when such property is held jointly by more than one person.

### **Vesting of Property in Central Government**

Section 9 provides that an order of confiscation made, in respect of any property of a person, vests in the Central Government all the rights and title in such property free from all incumbrances. The Adjudicating Authority after giving an opportunity of being heard to any other person interested in the property attached or seized is of the opinion that any encumbrances on the property or lease hold interest has been created with a view to defeat the provisions of the Act, it may, by order declare such encumbrances or lease hold interest to be void and thereupon the property shall vest in the Central Government free from such encumbrances or lease hold. However, this provision shall not discharge any person from any liability in respect of such encumbrances which may be enforced against such person by a suit for damages.

### **Obligation of Banking Companies, Financial Institutions and Intermediaries**

Chapter IV of the Act deals with obligations of Banking companies, financial institutions and intermediaries. Section 12 requires every banking company, financial institution and intermediary to maintain a record of all

transactions, the nature and value of which may be prescribed, whether such transactions comprise of a single transaction or a series of transactions legally connected to each other, and when such series of transactions take place within a month. These informations are required to be furnished to the Director within such time as may be prescribed. Banks and financial institutions are required to verify and maintain the records of the identity of all its clients, in such manner as may be prescribed. The records as mentioned above are required to be maintained for a period of ten years from the date of cessation of the transactions between the clients and the banking company, financial institution or intermediary.

Section 13 states that the Director may, either on his own motion, or on an application made by any authority, officer, or person, call for records of all transactions and make such inquiry or cause such inquiry to be made, as he thinks fit. In the course of any inquiry, if the Director finds that a banking company, financial institution or an intermediary or any of its officers has failed to maintain or retain records in accordance with the provisions of the Act, he may, by an order, levy a fine on such banking company, financial institution or intermediary which shall not be less than ten thousand rupees but may extend to one lakh rupees for each failure.

Section 15 empowers the Central Government to prescribe, in consultation with the Reserve Bank of India, the procedure and the manner of maintaining and furnishing information for the purpose of implementation of the provisions of the Act.

### **Summon, Searches and Seizures, etc.**

Section 16 empowers an authority to enter, on having reason to believe that an offence under Section 3 has been committed, any place within the limits of the area assigned to him or in respect of which he is authorised. Section 16(3) requires such authority to place marks of identification on the records inspected by him and make or cause to be made extracts or copies therefrom, make an inventory of any property checked or verified by him and record the statement of any person present in the place which may be useful for, or relevant to, any proceedings under the Act.

Section 18 of the Act deals with search of persons and provides that if an authority authorised in this behalf by the Central Government by general or special order has reason to believe that any person has secreted about his person or in anything under his possession, ownership or control any record or proceeds of crime which may be useful for or relevant to any proceedings under this Act, he may search that person and seize such record or property which may be useful for or relevant to any proceedings under this Act.

### **Retention of Property**

Section 20 of the Act deals with retention of property. As per Sub-section (1) provides that where any property has been seized under section 17 or section 18 or frozen under sub-section (1A) of section 17 and the officer authorised by the Director in this behalf has, on the basis of material in his possession, reason to believe (the reason for such belief to be recorded by him in writing) that such property is required to be retained for the purposes of adjudication under section 8, such property may, if seized, be retained or if frozen, may continue to remain frozen, for a period not exceeding one hundred and eighty days from the day on which such property was seized or frozen, as the case may be.

(2) The officer authorised by the Director shall, immediately after he has passed an order for retention or continuation of freezing of the property for purposes of adjudication under section 8, forward a copy of the order along with the material in his possession, referred to in sub-section (1), to the Adjudicating Authority, in a sealed envelope, in the manner as may be prescribed and such Adjudicating Authority shall keep such order and material for such period as may be prescribed.

(3) On the expiry of the period specified in sub-section (1), the property shall be returned to the person from whom such property was seized or whose property was ordered to be frozen unless the Adjudicating Authority permits retention or continuation of freezing of such property beyond the said period.

(4) The Adjudicating Authority, before authorising the retention or continuation of freezing of such property beyond the period specified in sub-section (1), shall satisfy himself that the property is *prima facie* involved in money-laundering and the property is required for the purposes of adjudication under section 8.

(5) After passing the order of confiscation under sub-section (5) or sub-section (7) of section 8, the Court or the Adjudicating Authority, as the case may be, shall direct the release of all property other than the property involved in money-laundering to the person from whom such property was seized or the persons entitled to receive it.

(6) Where an order releasing the property has been made by the Court under sub-section (6) of section 8 or by the Adjudicating Authority under section 58B or sub-section (2A) of section 60, the Director or any officer authorised by him in this behalf may withhold the release of any such property for a period of ninety days from the date of such order, if he is of the opinion that such property is relevant for the appeal proceedings under the Act.

### **Retention of records**

Section 21 deals with retention of records. Section 21(1) states that where any records have been seized, under section 17 or section 18 or frozen under sub-section (1A) of section 17 and the Investigating Officer or any other officer authorised by the Director in this behalf has reason to believe that any of such records are required to be retained for any inquiry under this Act, such records may if seized, be retained or if frozen, may continue to remain frozen, for a period not exceeding one hundred and eighty days from the day on which such records were seized or frozen, as the case may be.

(2) The person, from whom records seized or frozen, shall be entitled to obtain copies of records.

(3) On the expiry of the period specified under sub-section (1), the records shall be returned to the person from whom such records were seized or whose records were ordered to be frozen unless the Adjudicating Authority permits retention or continuation of freezing of such records beyond the said period.

(4) The Adjudicating Authority, before authorising the retention or continuation of freezing of such records beyond the period specified in sub-section (1), shall satisfy himself that the records are required for the purposes of adjudication under section 8.

(5) After passing of an order of confiscation under sub-section (5) or subsection (7) of section 8, the Adjudicating Authority shall direct the release of the records to the person from whom such records were seized.

(6) Where an order releasing the records has been made by the Court under subsection (6) of section 8 or by the Adjudicating Authority under section 58B or subsection (2A) of section 60, the Director or any officer authorised by him in this behalf may withhold the release of any such record for a period of ninety days from the date of such order, if he is of the opinion that such record is relevant for the appeal proceedings under the Act.

### **Presumption in Inter-connected Transactions**

Section 23 of the Act deals with presumption in inter-connected transactions and provides that where money laundering involves two or more transactions and one or more such transactions is or are proved to be

involved in money laundering, then for the purposes of adjudication or confiscation under Section 8, it shall be presumed that the remaining transactions form part of such interconnected transactions, unless otherwise proved to the satisfaction of the Adjudicating Authority.

### **Appellate Tribunal**

Chapter VI of the Act deals with Appellate Tribunal. Section 25 empowers the Central Government, to establish an Appellate Tribunal to hear appeals against the orders of Adjudicating Authority and other authorities under the Act.

### **Special Courts**

Sections 43 to 47 of the Act deal with provisions relating to Special Courts. Section 43(1) empowers the Central Government to designate, in consultation with the Chief Justice of the High Court, one or more Courts of Session as Special Courts or Court for such area or areas or for such case or class or group of cases as may be specified in the notification, for trial of offence punishable under Section 4.

### **Offences Triable by Special Courts**

Section 44(1) provides that the offence punishable under Section 4, shall be triable only by the Special Court constituted for the area in which the offence has been committed or a special court may, upon a complaint made by an authority authorised in this behalf take cognizance of the offence for which the accused is committed to it for trial.

### **Offences to be cognizable and Non-bailable**

Section 45 declares every offence punishable under the Act to be cognizable. It provides that notwithstanding anything contained in the Code of Criminal Procedure, 1973, a person accused of an offence punishable for a term of imprisonment of more than three years under Part A of the Schedule shall not be released on bail or on his own bond unless the Public Prosecutor has been given an opportunity to oppose the application for such release; and where the Public Prosecutor opposes the application, unless the Court is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while in bail.

However the special court shall not take cognizance of any offence punishable under Section 4, except upon a complaint in writing made by (i) the Director or (ii) any officer of the Central Government or State Government authorised in writing in this behalf by the Central Government by a general or special order made by that Government.

Sub-section 1A inserted by Prevention of Money Laundering (Amendment) Act, 2005 provides that notwithstanding anything contained in Code of Criminal Procedure, 1973 or any other provision of this Act, no police officer shall investigate into an offence under this Act, unless specifically authorized, by the Central Government by a general or special order, and subject to such conditions as may be prescribed.

### **Power of Central Government to Issue Directions**

Section 52 empowers the Central Government to issue, from time to time, such orders, instructions and directions to the authorities as it may deem fit for the proper administration of this Act. The authorities and all other persons employed in execution of the Act have been put under obligation to observe and follow such orders, instructions and directions of the Central Government. However, no such orders, instructions or directions shall be issued so as to require any authority to decide a particular case in a particular manner or interfere with the discretion of the Adjudicating Authority in exercise of his functions.

### **Agreement with Foreign Countries**

Section 56 empowers the Central Government to enter into an agreement with the Government of any country for enforcing the provisions of the Act and also for exchange of information for the prevention of any offence under the this Act or under the corresponding law in force in that country or investigation of cases relating to any offence under the Act.

### **Assistance to a Contracting State in Certain Cases**

Section 58 provides that, where a letter of request is received by the Central Government, from a court or authority in a contracting State requesting for investigation into an offence or proceedings under the Act and forwarding to such court or authority any evidence connected therewith, the Central Government may forward such letter of request to the Special Court or to any authority as it thinks fit for execution of such request in accordance with the provisions of the Act or as the case may be, any other law for the time being in force. Section 58A empowering Special Court to release the property.

### **Reciprocal Arrangements for Processes and Assistance for Transfer of Accused Persons**

Section 59(1) prescribes that where Special Court, in relation to an offence punishable under Section 4 desires that a summon to an accused person; or a warrant for the arrest of an accused person; or a summon to any person requiring him to attend and produce a document or other thing, or to produce a document or other things or to produce it; or a search warrant issued by it, shall be served or executed at any place in any contracting state, it shall send such summons or warrant in duplicate in such form, to such court, Judge or Magistrate through such authorities as the Central Government may by notification, specify in that behalf and that court, Judge or Magistrate, as the case may be, shall cause the same to be executed.

Sub-Section (2) stipulates that where a Special Court, in relation to an offence punishable under Section 4 has received for service or execution, summon to an accused person; or a warrant for the arrest of an accused person; or a summon to any person requiring him to attend and produce a document or other things or to produce it; or a search warrant; issued by a court, Judge or Magistrate in a contracting State, it shall cause the same to be served or executed as if it were a summon or warrant received by it from another court in the said territories for service or execution within its jurisdiction. Where a warrant of arrest has been executed, the person arrested shall, so far as possible be dealt with in accordance with the procedure specified under Section 19 and where a search warrant has been executed, the things found in the search shall so far as possible be dealt with in accordance with the procedure specified under Section 17 or 18.

However, where a summon or search warrant received from a contracting state has been executed, the documents or other things produced or things found in the search shall be forwarded to the court issuing the summon or search warrant through such authority as the Central Government may by notification specify in this behalf.

### **Attachment, Seizure and Confiscation of Property, etc.**

Section 60(1) provides that where the Director has made an order for attachment of any property under Section 5 or where Adjudicating Authority has made an order confirming such attachment or confiscation of any property under Section 8 and such property is suspected to be in a contracting state, the Special Court on an application by the Director or the Administrator appointed under Section 10(1) as the case may be, may issue a letter of request to a court or an authority in the contracting state for execution of such order.

Section 60(2) prescribes that when a letter of request is received by the Central Government from a court or an authority in a contracting state requesting attachment or confiscation of the property in India derived or obtained directly or indirectly, by any person from the commission of an offence under Section 3 committed

in that contracting state, the Central Government may forward such letter of request to the Director as it thinks fit, for execution in accordance with the provisions of the Act. Sub-Section (3) stipulates that the Director shall on receipt of a letter of request under Section 58 or Section 59 direct any authority under the Act to take all steps necessary for tracing and identifying such property.

### **(KYC) Norms/ (AML) Measures/ (CFT) Guidelines – Anti Money Laundering Standards**

RBI issued Master Circular on Know Your Customer (KYC) norms/Anti-Money Laundering (AML) standards/Combating of Financing of Terrorism (CFT)/Obligation of banks under Prevention of Money Laundering Act, (PMLA), 2002 and Banks were advised to follow certain customer identification procedure for opening of accounts and monitoring transactions of a suspicious nature for the purpose of reporting it to appropriate authority. These 'Know Your Customer' guidelines have been revisited in the context of the Recommendations made by the Financial Action Task Force (FATF) on Anti Money Laundering (AML) standards and on Combating Financing of Terrorism (CFT). Banks have been advised to ensure that a proper policy framework on 'Know Your Customer' and Anti-Money Laundering measures with the approval of the Board is formulated and put in place.

### **The objective of KYC Norms/ AML Measures/ CFT Guidelines**

The objective of Know Your Customer (KYC) Norms/Anti-Money Laundering (AML) Measures/Combating of Financing of Terrorism (CFT) guidelines is to prevent banks from being used, intentionally or unintentionally, by criminal elements for money laundering or terrorist financing activities. KYC procedures also enable banks to know/understand their customers and their financial dealings better which in turn help them manage their risks prudently.

### **Obligation of Banks**

- Banks should keep in mind that the information collected from the customer for the purpose of opening of account is to be treated as confidential and details thereof are not to be divulged for cross selling or any other like purposes. Banks should, therefore, ensure that information sought from the customer is relevant to the perceived risk, is not intrusive, and is in conformity with the guidelines issued in this regard. Any other information from the customer should be sought separately with his/her consent and after opening the account.
- Banks should ensure that any remittance of funds by way of demand draft, mail/telegraphic transfer or any other mode and issue of travellers' cheques for value of Rupees fifty thousand and above is effected by debit to the customer's account or against cheques and not against cash payment.
- Banks should ensure that the provisions of Foreign Contribution (Regulation) Act, 1976 as amended from time to time, wherever applicable are strictly adhered to.

### **KYC Policy**

Banks should frame their KYC policies incorporating the following four key elements:

- Customer Acceptance Policy;
- Customer Identification Procedures;
- Monitoring of Transactions; and
- Risk Management.

### **For the purpose of KYC policy, a 'Customer' is defined as:**

- a person or entity that maintains an account and/or has a business relationship with the bank;

- one on whose behalf the account is maintained (i.e. the beneficial owner);
- beneficiaries of transactions conducted by professional intermediaries, such as Stock Brokers, Chartered Accountants, Solicitors etc. as permitted under the law, and
- any person or entity connected with a financial transaction which can pose significant reputational or other risks to the bank, say, a wire transfer or issue of a high value demand draft as a single transaction.

### **Introduction of New Technologies – Credit cards/debit cards/ smart cards/gift cards**

Banks should pay special attention to any money laundering threats that may arise from new or developing technologies including internet banking that might favour anonymity, and take measures, if needed, to prevent their use in money laundering schemes. Many banks are engaged in the business of issuing a variety of Electronic Cards that are used by customers for buying goods and services, drawing cash from ATMs, and can be used for electronic transfer of funds. Banks are required to ensure full compliance with all KYC/AML/CFT guidelines issued from time to time, in respect of add-on/ supplementary cardholders also. Further, marketing of credit cards is generally done through the services of agents. Banks should ensure that appropriate KYC procedures are duly applied before issuing the cards to the customers. It is also desirable that agents are also subjected to KYC measures.

### **Information to be preserved**

Banks are required to maintain all necessary information in respect of transactions to permit reconstruction of individual transaction, including the following information:

- (a) the nature of the transactions;
- (b) the amount of the transaction and the currency in which it was denominated;
- (c) the date on which the transaction was conducted; and
- (d) the parties to the transaction

### **Maintenance and Preservation of record**

- (a) Banks are required to maintain the records containing information of all transactions. Banks should take appropriate steps to evolve a system for proper maintenance and preservation of account information in a manner that allows data to be retrieved easily and quickly whenever required or when requested by the competent authorities.
- (b) Banks should ensure that records pertaining to the identification of the customer and his address (e.g. copies of documents like passports, identity cards, driving licenses, PAN card, utility bills etc.) obtained while opening the account and during the course of business relationship, are properly preserved. The identification records and transaction data should be made available to the competent authorities upon request.
- (c) Banks have been advised to pay special attention to all complex, unusual large transactions and all unusual patterns of transactions, which have no apparent economic or visible lawful purpose. It is further clarified that the background including all documents/office records/memorandums pertaining to such transactions and purpose thereof should, as far as possible, be examined and the findings at branch as well as Principal Officer level should be properly recorded. Such records and related documents should be made available to help auditors in their day-to-day work relating to scrutiny of transactions and also to Reserve Bank/other relevant authorities.

## Reporting to Financial Intelligence Unit – India

In terms of the PMLA Rules, banks are required to report information relating to cash and suspicious transactions and all transactions involving receipts by non-profit organisations of value more than rupees ten lakh or its equivalent in foreign currency to the Director, Financial Intelligence Unit-India (FIU-IND) in respect of transactions.

## Freezing of Assets under Section 51A of Unlawful Activities (Prevention) Act, 1967

The Unlawful Activities (Prevention) Act, 1967 (UAPA) has been amended by the Unlawful Activities (Prevention) Amendment Act, 2012. Government has issued an Order dated August 27, 2009 detailing the procedure for implementation of Section 51A of the Unlawful Activities (Prevention) Act, 1967 relating to the purposes of prevention of, and for coping with terrorist activities. In terms of Section 51A, the Central Government is empowered to freeze, seize or attach funds and other financial assets or economic resources held by, on behalf of or at the direction of the individuals or entities Listed in the Schedule to the Order, or any other person engaged in or suspected to be engaged in terrorism and prohibit any individual or entity from making any funds, financial assets or economic resources or related services available for the benefit of the individuals or entities Listed in the Schedule to the Order or any other person engaged in or suspected to be engaged in terrorism.

## LESSON ROUND-UP

- Money laundering is the processing of criminal proceeds to disguise its illegal origin.
- The process of money laundering can be classified into three stages, namely, placement, layering and integration.
- The Prevention of Money-laundering Act, 2002 was enacted to prevent money laundering and to provide for confiscation of property derived from, or involved in, money laundering and for matters connected therewith or incidental thereto.
- The Act also addresses the international obligations under the Political Declaration and Global Programme of Action adopted by the General Assembly of the United Nations to prevent money laundering.
- The Act contains provisions pertaining to offences and punishment for money laundering, attachment, adjudication and confiscation, obligations of banking companies, financial institutions and intermediaries, Summons, Searches and Seizures etc.
- The Act states that whoever, acquires, owns, possesses, or transfers any proceeds of crime or knowingly enters into any transaction which is related to proceeds of crime directly or indirectly or conceals or aids in the concealment of the proceeds of crime, shall be guilty of offence of money laundering.
- Every banking company, financial institution and intermediary is required to maintain a record of all transactions, the nature and value of which may be prescribed, whether such transactions comprise of a single transaction or a series of transactions legally connected to each other, and when such series of transactions take place within a month.
- The objective of Know Your Customer (KYC) Norms/Anti-Money Laundering (AML) Measures/Combating of Financing of Terrorism (CFT) guidelines is to prevent banks from being used, intentionally or unintentionally, by criminal elements for money laundering or terrorist financing activities. KYC procedures also enable banks to know/understand their customers and their financial dealings better which in turn help them manage their risks prudently.

## SELF-TEST QUESTIONS

1. Define the term money laundering and explain the process of money laundering.
  2. Briefly discuss the international efforts in preventing the money laundering.
  3. Briefly explain the salient features of Prevention of Money Laundering Act.
  4. Write short note on the following:
    - (a) Impact of money laundering on the Development.
    - (b) Obligation of banking companies, financial institutions and intermediaries.
    - (c) Attachment, seizure and confiscation of property etc.
  5. What are the objectives of KYC guidelines and when does KYC norms apply?

# Lesson 10

## LAW RELATING TO ESSENTIAL COMMODITIES, WEIGHTS AND MEASURES

### (ESSENTIAL COMMODITIES ACT, 1955)

#### Section I

#### LESSON OUTLINE

- Overview of Essential Commodities Act, 1955
- Object and Scope of the Act
- Essential Commodities
- Powers of Central Government to control production, supply and distribution etc., of essential commodities
- Fixing of price for essential commodities
- Seizure of Essential Commodities
- Confiscation of Essential Commodities
- Appeal against Confiscation
- Orders passed under Essential Commodities Act, 1955
- Offences and penalties
- Grant of Injunction by Civil Court
- Culpable Mental State
- Offences by companies
- Publication of names of convicted companies
- Attempt and abetment

#### LEARNING OBJECTIVES

The Essential Commodities Act, 1955 was enacted to ensure easy availability of essential commodities to the consumers and to protect them from exploitation by unscrupulous traders. The Act provides for regulation and control of production, distribution and pricing of commodities, which are declared as essential for maintaining or increasing supplies or for securing their equitable distribution and availability at fair prices'.

The Essential Commodities Act is being implemented by the State Governments/UT Administrations by availing of the delegated powers under the Act. The State Governments/UT Administrations have issued various Control Orders for regulation, production and distribution of Essential Commodities such as food grains, edible oils, pulses kerosene, sugar etc. The Central Government regularly monitors the action taken by State Governments/UT Administrations to implement the provisions of the Essential Commodities Act, 1955.

The items declared as essential commodities under the Essential Commodities Act, 1955 are reviewed from time to time in the light of liberalized economic policies in consultation with the Ministries/Departments administering the essential commodities and particularly with regard to their production, demand, and supply.

The preamble to the Act says that it is an Act to provide in the Interest of the general Public for the control of production, supply and distribution of, and trade and commerce in, certain commodities.

## INTRODUCTION

In 1939 the Government of India made certain rules to control the production, supply and distribution of certain commodities under the Defence of India Act which ceased to have force in September, 1946. It was however considered necessary that control in respect of certain commodities essential for human beings should continue in the interest of the general public. Therefore, the Essential Supplies (Temporary Powers) Ordinance, XVIII of 1946 was promulgated by which certain provisions of the Defence of India Rules continued to have force. This Ordinance was subsequently replaced by the Essential Supplies (Temporary Powers) Act, 1946 (Act No. XXIV of 1946).

The operation of the Act was prolonged upto 1st April, 1948, by virtue of a Notification published in the Gazette of India, dated March 8, 1947. Under certain resolution of the Constituent Assembly passed in 1948 and 1949 and by the Adaptation of Laws Act, 1950, the operation of the Act was further extended to different periods from time to time.

Since in public interest it was considered necessary that the Centre should continue to control production, supply and distribution of certain essential commodities, the need for a permanent measure on the subject was felt. For this purpose, certain amendments were required to be made in the Constitution. The Constitution (Third Amendment) Act made the required amendments in Entry 33 of List 3 of the Seventh Schedule to the Constitution to enable the Parliament to enact the required legislation. The Essential Commodities Ordinance No. 1 of 1955, was therefore, promulgated which came into force on 26th January, 1955. This Ordinance was subsequently replaced by the present Act namely, the Essential Commodities Act, 1955 (Act No. 1 of 1955) w.e.f 1st April, 1955.

## OBJECT AND SCOPE OF THE ACT



*The Preamble to the Act says that it is an Act to provide in the interest of the general public for the control of the production, supply and distribution of, and trade and commerce in, certain commodities. The dominant object and intendment of the Act is to secure equitable distribution and availability at fair prices of essential commodities in the interest of the general public. The interest of the general public necessarily connotes the interest of the consuming public and not the interest of the dealer (1958 Andh. LT587).*

## DEFINITIONS (SECTION 2)

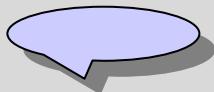
The Act contains definitions of five important terms, namely:

### **Collector**

“Collector” includes an Additional Collector, and such other officer not below the rank of sub-divisional Officer as may be authorised to perform the functions and exercise the powers of the Collector under the Act [Section 2(ia)].

### **Essential Commodities**

Section 2A dealing with Essential commodities declaration, etc. defines the "essential commodity" as to mean a commodity specified in the Schedule.

**Schedule to the Act lists out following commodities:**

- (1) *drugs: The explanation clarifies that for the purposes of this Schedule, "drugs" has the meaning assigned to it in clause (b) of Section 3 of the Drugs and Cosmetics Act, 1940 (23 of 1940);*
- (2) *fertilizer, whether inorganic, organic or mixed;*
- (3) *foodstuffs, including edible oilseeds and oils;*
- (4) *hank yarn made wholly from cotton;*
- (5) *petroleum and petroleum products;*
- (6) *raw jute and jute textiles;*
- (7) (i) *seeds of food-crops and seeds of fruits and vegetables;*  
 (ii) *seeds of cattle fodder; and*  
 (iii) *jute seeds.*

Sub-section (2) empowers the Central Government to amend, if it is satisfied that it is necessary so to do in the public interest and for reasons to be specified in the notification published in the Official Gazette, the Schedule so as to (a) add a commodity to the said Schedule; and (b) remove any commodity from the said Schedule, in consultation with the State Governments.

In terms of Sub-section (3) any notification issued under Sub-section (2) may also direct that an entry shall be made against such commodity in the said Schedule declaring that such commodity shall be deemed to be an essential commodity for such period not exceeding six months to be specified in the notification. However, Central Government may, in the public interest and for reasons to be specified, by notification in the Official Gazette, extend such period beyond the said six months.

The Central Government may exercise its powers under Sub-section (2) in respect of the commodity to which Parliament has power to make laws by virtue of Entry 33 in List III in the Seventh Schedule to the Constitution. Every notification issued under sub-section (2) is required to be laid, as soon as may be after it is issued, before both Houses of Parliament.

In addition to the items included in the list given in the said clause, such other items which may be so declared by the Central Government by notified orders would also be included in the list of essential commodities, but in any case, such commodities would not be outside the scope of Entry 33 in List III in the Seventh Schedule to the Constitution. The Central Government has time and again, notified various commodities to be essential commodities. The term 'essential commodities' is defined in Rule 35(3) of the Defence of India Rules, 1962, to mean "food, water, fuel, light, power or any other thing notified by the Central Government in this behalf as essential for the existence of the community". Of course, the definition in the Essential Commodities Act is more comprehensive than that in the Defence of India Rules, but both definitions enumerate certain things or articles and have scope for addition to the list of other articles notified in that behalf by the Central Government. As such, the articles not expressly mentioned in the definition given in the Defence of India Rules, can become essential commodities within the meaning of the expression used in the Rules by a simple government notification and the slight difference in the definition of essential commodity in the Act from that given in the Rules does not make one repugnant to the other [Nathuni Lai Gupta v. The State (1964 Cr. LJ 662)].



*IN S. Samuel, AID. Harrisons Malayava v. Union of India, AIR 2004 SC 218, Supreme Court held that Tea is not foodstuff. Even in a wider sense, foodstuffs will not include tea as tea either in the form of the leaves or in the form of beverage, does not go into the preparation of food proper to make it more palatable and digestible. Tea leaves are not eaten. Tea is a beverage produced by steeping tea leaves or buds of the tea plants in the boiled water. Such tea is consumed hot or cold for its flavour, taste and its quality as a stimulant. The stimulating effect is caused by the presence of caffeine therein. Tea neither nourishes the body nor sustains nor promotes its growth. It does not have any nutritional value. It does not help formation of enzymes nor does it enable anabolism. Tea or its beverage does not go into the preparation of any foodstuff. In common parlance, any one who has taken tea would not say that he has taken or eaten food. Thus tea is not a food.*

- **Order:** “Order” includes a direction issued thereunder [Section 2(c)].
- **State Government:** “State Government”, in relation to a Union territory means the administrator of such territory [Section 2(d)].
- **Sugar:** “Sugar” means: (i) any form of sugar containing more than 90 per cent of sucrose, including sugar candy; (ii) Khandsari sugar or bura sugar or crushedsugar, or any sugar in crystalline or powdered form; or (iii) sugar in process in vacuum pan sugar factory, or raw sugar [Section 2(e)].

### Authorities responsible to administer the Act

Necessary powers have been given to the Central Government under the Act to administer the provisions of the Act by issuing orders/directions notified in the official gazette and by delegating the authority to State Governments and administrators of Union Territories. The Central Government at its apex level is responsible for achieving the objectives enshrined by the Parliament under this Act for the welfare and general well-being of all the citizens.

### Powers of Central Government to control production, supply and distribution etc., of essential commodities [Section 3]



#### Power to Issue Orders

*The Central Government having been vested with power under Section 3(1) can issue order in the following circumstances providing for regulating or prohibiting the production, supply and distribution of essential commodities and trade and commerce therein:*

- when it is necessary or expedient for maintaining or increasing supplies of any essential commodity;*
- for securing the equitable distribution and availability of essential commodities at fair price; or*
- for securing any essential commodity for the defence of India or the efficient conduct of military operations.*

## Contents of the Order

Notwithstanding the above and without prejudice to the generality of the powers contained in Sub-section (1) above, Sub-section (2) of Section 3 provides that the Central Government may issue an order which may provide for all or any of the following matters:

- (a) for regulating by licences, permits or otherwise the production or manufacture of any essential commodity;
- (b) for bringing under cultivation any waste or arable land, whether appurtenant to a building or not, for growing thereon of food crops generally or of specified food crops and for otherwise maintaining or increasing the cultivation of food crops generally, or of specified foodcrops;
- (c) for controlling the price at which any essential commodity may be bought or sold.
- (d) for regulating by licences, permits or otherwise the storage, transport, distribution, disposal, acquisition, use or consumption of any essential commodity;
- (e) for prohibiting the withholding from sale of any essential commodity ordinarily kept for sale;
- (f) for requiring any person holding in stock, or engaged in the production, or in the business of buying or selling, of any essential commodity—(a) to sell the whole or a specified part of the quantity held in stock or produced or received by him, or (b) in the case of any such commodity which is likely to be produced or received by him, to sell the whole or a specified part of such commodity when produced or received by him, to the Central Government or a State Government or to an officer or agent of such Government or to a Corporation owned or controlled by such Government or to such other person or class of persons and in such circumstances as may be specified in the order.

Explanation I provides that an order made under this clause in relation to foodgrains, edible oilseeds or edible oils may, having regard to the estimated production, In the concerned area, of such foodgrains, edible oilseeds and edible oils, fix the quantity to be sold by the producers in such area and may also fix, or provide for the fixation of such quantity on a graded basis, having regard to the aggregate of the area held by, or under the cultivation of the producers. Explanation II provides that “production” for the purposes of this clause includes manufacture of edible oils and sugar with its grammatical variation and cognate expressions;

- (g) for regulating or prohibiting any class of commercial or financial transactions relating to foodstuffs which in the opinion of the authority making the order, are, or if unregulated, are likely to be detrimental to the public interest;
- (h) for collecting any information or statistics with a view to regulating or prohibiting any of the aforesaid matters;
- (i) for requiring persons engaged in the production of, or trade and commerce in, any essential commodity to maintain and produce for inspection such books, accounts and record relating to their business and to furnish such information relating thereto as may be specified in the order;
- (j) for the grant or issue of licences, permits or other documents, the charging of fees therefor, the deposit of such sum, if any, as may be specified in the order as security for the due performance of the conditions of any such licence, permit or other document, the forfeiture of the sum so deposited or any part thereof for contravention of any such conditions and the adjudication of such forfeiture by such authority as may be specified in the order;
- (k) for any incidental and supplementary matters, including in particular, the entry, search or examination of premises, aircraft, vessels, vehicles or other conveyances and animals and the

seizure by a person authorised to make such entry, search or examination of any article in respect of which such person has reason to believe that a contravention of the order has been, is being or is about to be, committed and any packages, coverings, or receptacles in which such articles are found; (ii) of any aircraft, vessel, vehicle or other conveyance or animal used in carrying such articles, if such a person has reason to believe that such aircraft, vessel, vehicle or other conveyance or animal is liable to be forfeited under the provisions of this Act; (iii) of any books of account and documents which in the opinion of such person, may be useful to, or relevant to any proceeding under this Act and the person from whose custody such books of account or documents are seized shall be entitled to make copies thereof or to take extracts therefrom in the presence of an officer having the custody of such books of account or documents.

### **Fixing the Price of Essential Commodities being sold to Government**

Section 3(3) vests powers in Central Government to deal with the pricing of the essential commodities particularly when the commodities are being sold to Central/State Government in compliance of order under clause (f) of Sub-section (2) of Section 3. In such a case, the price shall be paid as provided hereunder:

- (a) the agreed price, where the price can be agreed upon consistently with the controlled price fixed under this section;
- (b) controlled price: where no such agreement can be reached, the price calculated with reference to controlled price;
- (c) the price calculated at the market rate prevailing in the locality on the date of sale, where neither clause (a) nor clause (b) applies.

### **Fixing the Price of Essential commodities during Emergency**

Section 3(3A)(i) is in the nature of an emergency provision and can be resorted to meet a situation arising at a particular locality. It empowers the Central Government to direct the price at which the foodstuffs in any locality will be sold to general public. This direction will be issued only when the Central Government is of the opinion that taking such step is necessary for controlling price rise or preventing the hoarding of any foodstuff in any locality. The notification issued by the Government to the above effect shall be in force for 3 months only as may be specified therein as per Sub-section (3A)(ii). Further, for selling specified foodstuffs in the specified locality, the seller shall be paid price therefor as follows:

- (a) agreed price, when the price can be agreed upon consistently with the controlled price fixed under this sub-section; or
- (b) the controlled price, when no such agreement can be reached as stated above; or
- (c) the market rate price as per the prevailing market rate in the locality at the date of sale where neither of the above clause (a) or (b) apply.

### **Payment of Procurement Price for Foodgrains and Edible Oil**

The Essential Commodities (Amendment) Act, 1976, inserted Sub-section (3B) in substitution of the then existing section providing for payment of procurement price of such foodgrains, edible oils or oilseeds as may be specified by State Government with the prior approval of Central Government. Therefore, as per Section 3(3B) where any person is required in terms of an order under Sub-section (2)(f) to sell to the Central Government or a State Government or any officer or agent of such Government or to a Corporation owned or controlled by such Government any grade or variety of foodgrains, edible oil and oilseeds in relation to which

no notification has been issued Under Section 3(3A) or such notification, having been issued, has ceased to be in force, procurement price shall be paid irrespective of the provisions of Sub-section (3) having regard to the following facts:

- (a) the controlled price, if any, fixed under this section or by or under any other law for the time being in force for such grade or variety of foodgrains, edible oils and oilseeds;
- (b) the general crop prospects;
- (c) the need for making such grade or variety of foodgrains, edible oils and seeds available at reasonable prices to the consumers, particularly the vulnerable sections of the consumers; and
- (d) the recommendations, if any, of the Agricultural Prices Commission with regard to the price of the concerned grade or variety of foodgrains, edible oils and oilseeds.

### **Fixing Price for Sugar to be Paid to Producer**

Sub-section (3C) of Section 3 provides that where any producer of sugar is required by an order made under Sub-section (2)(f) to sell any kind of sugar to the Central or State Government/officer or agent of such government or to any person/class of persons, whether notification in this regard under Sub-section (3A) is issued or not or ceased to be in force and notwithstanding anything contained in Sub-section (3), the producer shall be paid such price for sugar as the Central Government may, by order, determine having regard to (a) the minimum price, if any fixed for sugar cane by the Central Government under this section; (b) the manufacturing cost of sugar; (c) the duty or tax, if any, paid or payable thereon; and (d) the securing of a reasonable return on the capital employed in the business of manufacturing sugar.

Further, the Central Government may determine different prices for different areas from time to time or for different factories or for different kinds of sugar. It is explained in the sub-section that producers for the purposes of this sub-section shall include persons carrying on business of manufacturing sugar.

Price fixation under Section 3(2) and 3(3B) is different from price fixation in the case of sugar under Sub-section (3C). In the former, the dominant purpose in fixing price is to ensure that goods are available to consumers at a reasonable price. In the latter, price fixed must also give a reasonable return on investment to the producer.

Sub-section (3D) of the Act empowers the Central Government to direct that no producer, importer or exporter to sell or otherwise dispose of or deliver any kind of sugar or remove any kind of sugar from the bonded godowns of the factory in which it is produced, whether such godowns are situated within the premises of the factory or outside or from the warehouses of the importers or exporters, as the case may be, except under and in accordance with its direction. However, this provision does not affect the pledging of such sugar by any producer or importer in favour of any scheduled bank as defined in clause (e) of Section 2 of the Reserve Bank of India Act, 1934 or any corresponding new bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970, so, however, that no such bank sells the sugar pledged to it except under and in accordance with a direction issued by the Central Government.

In terms of Sub-section 3(E) the Central Government has been empowered to direct from time to time, by general or special order, any producer or importer or exporter or recognised dealer or any class of producers or recognised dealers, to take action regarding production, maintenance of stocks, storage, sale, grading, packing, marking, weighment, disposal, delivery and distribution of any kind of sugar in the manner specified in the direction.

### **Power to Appoint Authorised Controller**

The Central Government has been vested with necessary powers under Sub-section (4) of Section 3 to authorise any person (known as authorised controller) when it is considered necessary for maintaining or increasing the production and supply of essential commodities. The authorised controller shall exercise such functions of control as may be provided in the order with respect to the whole or any part of any such undertaking engaged in the production and supply of the commodity. The authorised controller shall exercise his functions in accordance with any instructions given to him by the Central Government. He shall not have any power to give any direction inconsistent with the provisions of any enactment or any instrument determining the functions of the person in charge of the management of the undertaking except in so far as may be specifically provided by the order. The undertaking shall be carried on in accordance with any directions, given by the authorised controller under the provisions of the order. The person who is responsible to function as a manager of the undertaking or part of it shall comply with such directions.

### **Issuance and Service of Order'**

An order made under Section 3 of the Act shall be issued and served in the manner as provided under Section 3(5) i.e. in the following manner:

- (a) in the case of an order of general nature or affecting a class of persons be notified in the official gazette; and
- (b) in the case of an order directed to a specified individual be served on such individual (i) by delivering or tendering it to that individual, or (ii) if it cannot be so delivered or tendered, by affixing it on the outer door or some other conspicuous part of the premises in which that individual lives, and a written report thereof shall be prepared and witnessed by two persons living in the neighbourhood.

### **Laying the Order before Parliament**

Sub-section (6) provides that every order made under Section 3 by the Central Government or by any officer or authority of Central Government shall be laid before both Houses of Parliament as soon as may be, after it is made.

### **Imposition of Duties on State Government**

Section 4 of the Act provides that an order made under Section 3 may confer powers and impose duties upon the Central Government or the State Government or officers and authorities of the Central Government or State Government and may contain directions to any, State Government or to officers or authorities thereof as to the exercise of any such powers or discharge of any such duties.

### **Delegation of powers**

In terms of Section 5, the Central Government may, by notified order direct that the power to make orders or issue notifications under Section 3 shall in relation to such matters and subject to such conditions, if any, as may be specified in the direction be exercisable also by (a) such officer or authority subordinate to Central Government, (b) such State Government or such officer or authority subordinate to a State Government as may be specified in the direction.

### **NATURE OF ORDER PASSED UNDER THE ACT**

It may be noted from the foregoing paragraphs that the order notified by the Government under Section 3(2) specifies the various aspects which may be covered under the order while ensuring the production, procurement and distribution of the essential commodities. Further, Sub-sections (3), (3A), (3B), (3C) provide

for issuance of order for fixation of prices of the essential commodities. Order may be passed for appointing Controlling Authority under this Act which is of different nature being administrative in kind and effect. Sub-section (5) provides for the issuance and service of the order. The order notified by the Government is such an important document that the Act provides, under Sub-section (6) of Section 3, for it to be placed before both Houses of Parliament. Thus, the order in its nature, is a medium of administering the Act and a proper course of communication to and from the Government, exercising and delegating the powers vested in the Government under the Act.

### **Effect of the Order**

Section 6 provides that the order made under Section 3 shall have effect notwithstanding anything inconsistent therewith contained in any enactment other than this Act or any instrument having effect by virtue of any enactment other than this Act.

It could be seen that this section does not either expressly or by implication, repeal any of the provisions of the pre-existing laws, nor does it abrogate such laws. The object of Section 6 is simply to bypass them. Thus, for example, an order made under Section 3 would be operative in regard to the essential commodities covered by the Textile Control Order, wherever there is any repugnancy in that order with any existing law, and to that extent the existing law with regard to those commodities will not operate.

The Calcutta High Court had observed that the ultimate effect of Section 6 is that an order under Section 3 will override existing laws, only on the ground that the are orders validly made under Section 3 of the Act (*Ramananda Agrawala v. State AIR 1951 Calcutta 120*).

As rightly pointed out by the Patna High Court, Section 6 is a saving section which affords protection to the orders made under Section 3 of the Act as against the onslaught of any law, merely by reason of inconsistency (*Mohammad Anwar Hussi v. State of Bihar, AIR 1955 Patna 220*).

### **Presumption as to Orders**

Section 13 provides that where an order purports to have been made and signed by an authority in exercise of any powers conferred by or under this Act, a court so presume that such order was so made by that authority within the meaning of Indian Evidence Act, 1972.

### **Burden of Proof in certain cases**

Section 14 provides that on being prosecuted for contravention of any order made under Section 3 which prohibits him from doing any act or being in possession of a thing without lawful authority or without a permit, licence or other document such person shall have to prove that he has such authority, permit, licence or other document as the burden of proof lies upon him.

### **Protection for Acts done in Pursuance of Order**

Section 15 provides immunity against action taken in good faith under the Act and lays down that no suit, prosecution or other legal proceedings can be taken against any person for anything which is in good faith done, or intended to be done, in pursuance of any order made under Section 3 of the Act. Likewise, no suit or other legal proceedings can lie against the Government, for any damage caused or likely to be caused, by any thing which is in good faith done, or intended to be done, in pursuance of any order made under Section 3 of the Act.

It may be noted that immunity can be claimed by the Government or by its officers, only if it is shown that an order was issued under Section 3 of the Act, and the liability which the plaintiff is seeking to enforce arises from the fact that action was taken in pursuance of the order of the government under that section.

## CONFISCATION OF ESSENTIAL COMMODITIES

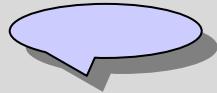
### Seizure and Confiscation of Essential Commodities

The Essential Commodities Act envisages two independent proceedings against a person charged with contravention of the provisions of the Act. Under Section 6A, the Collector can confiscate the seized commodity and under Section 7, the contravention would be punishable. Confiscation of essential commodities is a sharp weapon which the Act has provided to the Central Government under Section 6A of the Act.

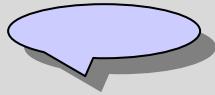
Section 6A provides that where any essential commodity is seized in pursuance of an order made under Section 3, a report of such seizure shall be made, without any unreasonable delay, to the collector of the district or the Presidency town in which such essential commodity is seized. The Collector at his discretion, may direct for the production of the seized commodity before him and if he is satisfied that there has been contravention of the order he may pass order for confiscation of (a) the essential commodity so seized, (b) any package, covering or receptacle in which such essential commodity is found, and (c) any animal, vehicle, vessel or other conveyance used in carrying such essential commodity. Provided that without prejudice to any action which may be taken under any other provision of this Act, no foodgrains or edible oilseeds seized in pursuance of an order made under Section 3 in relation thereto from a producer shall, if the seized foodgrains or edible oilseeds have been produced by him, be confiscated under this section. Provided further that in the case of any animal, vehicle, vessel or other conveyance the owner of such animal, vehicle etc., shall be given an option to pay in lieu of its confiscation, a fine not exceeding the market price at the date of seizure of the essential commodity sought to be carried by such animal, vehicle, vessel, or other conveyance.

The Act uses the expressions 'confiscation' and 'seizure' in Section 6A and under this section a commodity which has been seized in pursuance of an order under Section 3 can be confiscated under the circumstances mentioned in Section 6A. Therefore, it is essential to know in brief the distinction between seizure and confiscation.

#### 'Seizure'



*The expression 'seize' means to take possession contrary to the wishes of the owner of the property and that such action is unilateral action of the person seizing. The person from whom anything is seized loses, from the moment of seizure, the right or power to control or regulate the use of that thing. The dictionary meaning of the word 'seize' means to lay hold of suddenly or forcibly, to take hold of, to reach and grasp, to clutch'. It also means 'to take possession of or appropriate in order to subject to the force or operation of a warrant, order of Court or other legal processes. A reference to some provisions of the Codes of Criminal Procedure shows that the term seizure had been used therein in connection with the taking of actual physical possession of moveable property.*

**'Confiscation'**

**'Confiscation'** according to *Wharton's Law Lexicon*, is condemnation and adjudication of property to the public treasury as of goods seized under the Customs Act. Confiscation, according to *Stroud's Judicial Dictionary*, must be an act done in some way on the part of the Government of the country where it takes place and in some way beneficial to that Government, though the proceeds may not strictly speaking be brought into its treasury. In *State of Kerala v. Mathai* (1961 K.L.T. 169) it was pointed out that confiscation is not to be considered part of the sentence for an offence but is only a mode by which Courts can dispose of property which comes before it in criminal trials.

That being the general distinction between confiscation and seizure, in the context of the Essential Commodities Act, it could be seen that an essential commodity which has been seized, could be confiscated. Therefore, confiscation is an action posterior to the seizure of the essential commodity. A commodity that has not been seized cannot be confiscated. Seizure itself does not imply confiscation. The seizure should have been made by virtue of an order passed under Section 3 of the Act. Clause (j) of Section 3 empowers the Government to make an order for seizure of any essential commodity if an order made by the Central Government controlling production, supply, distribution etc. of essential commodities has been or is about to be contravened. Therefore, any contravention or intended contravention of an order passed by the Government under the Act may lead to seizure, and under the circumstances mentioned in Section 6A such seized commodity could be confiscated.

Power is conferred on the Collector to confiscate any Animal, vehicle, vessel or other conveyance if used in carrying the essential commodities. Where it was clear from the report of the Sub-Inspector of Police that the jeep in question was not found or used for carrying any essential commodity, it was found moving in front of the lorry which was loaded with paddy, it was held that, that by itself was no ground for its seizure. Unless the vehicle was used for carrying the essential commodities, the Deputy Commissioner had no jurisdiction to initiate proceedings for its confiscation, much less the police to seize it. [*Ramchandra v. Sub-Inspector of Police* (1976) 1 Kar. LJ. 126]

The Collector has no jurisdiction to go into the validity of the seizure; he could only confiscate goods, out of those seized, in respect of which contravention is established. Only if the seizure is valid could the Collector have jurisdiction to go on into the question whether there has been any contravention of the control order in respect of the whole or part of the goods, seized at this is entirely different from saying that the Collector could go on with the enquiry, postulated in Sections 6A and 6B, when the seizure itself, on which alone his jurisdiction to make an enquiry depends, is found to be illegal. [*Hindustan Aluminium v. Controller of Aluminium*, AIR (1976) DeWii225]

In *S. Seetharamayya Gupta v. Distt. Revenue Officer, Chittoor* (AIR 1977 AP 103) it was held that delegation of power of the Collector under Section 6A to Distt. Officer is competent and valid. Even though Section 6A authorizes confiscation of seized goods it does not say that the entire seized quantity should be directed to the confiscated. It is left to the discretion of the Distt. Revenue Officer and the appellate authority to decide whether the entire seized stock should be confiscated or only a portion of it. That, however, is a judicial discretion and must be exercised judicially having regard to the circumstances of the case, the gravity of the matter and other relevant and pertinent factors. The Act provides for enquiry and total absence of adequate opportunity to the party to make representation and consequently passing order of confiscation must be held bad.

### **Sale of the Confiscated Commodity**

Section 6A(2) provides that where the collector, on receiving a report of seizure or on inspection of any essential commodity under Sub-section (1) above, is of the opinion that the essential commodity is subject to speedy and natural decay or it is otherwise expedient in the public interest so to do he may (i) order the same to be sold at the controlled price, if any, fixed for such essential commodity under this Act or under any other law for the time being in force; (ii) where no such price is fixed, order the same to be sold by public auction. Provided that in case of foodgrains, the collector may, for its equitable distribution and availability at fair prices, order the same to be sold through fair price shops at the price fixed by the Central Government or by the State Government as the case may be, for the retail sale of such foodgrains to the public.

### **Disposal of Sale Proceeds of Confiscated Goods**

In terms of Section 6A(3), the sale proceeds of the essential commodity sold, after deduction of the expenses of any such sale or auction or other incidental expenses relating thereto shall be paid to the owner or person from whom it is seized in the following circumstances: (a) where no order of confiscation is ultimately passed by the Collector; (b) where an order passed on appeal under Sub-section (1) of Section 6C so requires, or (c) where in a prosecution instituted for the contravention of the order in respect of which an order of confiscation has been made under this section, the person concerned is acquitted.

### **Issue of Show Cause Notice before Confiscation of Essential Commodity**

Before passing an order for confiscation under Section 6A, in terms of Sub-section (1) of Section 6B of the Act, the owner of the essential commodity, package, covering, receptacle, animal, vehicle, vessel or other conveyance or the person from whom it is seized is required to be given a notice in writing informing him of the grounds on which it is proposed to confiscate the above goods to provide him an opportunity of making a representation in writing within a reasonable time and give him a reasonable opportunity of being heard in the matter.

It is also provided in Sub-section (2) that no order of confiscation can be made if the owner of the confiscated animal, vehicle, vessel or other conveyance proves to the satisfaction of the Collector that the said modes of transport owned by him were used in carrying the essential commodity without his knowledge or connivance of himself or his agent, if any, and each of them had taken the necessary precautions against such use.

It is not sufficient for the owner to prove that the vehicle carried the essential commodity without his knowledge or concurrence. He must also prove that the vehicle was used without the knowledge, or concurrence of the person in charge of the vehicle. In addition, he must prove that not only he but also the person in charge of the vehicle had taken all reasonable and necessary precautions against such use [*Shai Rahhim v. State of Andhra* (1976) LT 357].

However, once an order confiscating the goods of above description has been passed it shall not be held invalid in terms of Sub-section (3) merely by reason of any defect or irregularity in the notice given under clause (a) of Sub-section (1) if in giving such notice the provisions of that clause have been substantially complied with.

### **Appeal against Confiscation Order**

In terms of Sub-section (1) of Section 6C, any person aggrieved by an order of confiscation under Section 6A may appeal to the State Government concerned within one month from the date of passing the order. The State Government shall give an opportunity to the appellant to be heard and pass such order as it may think fit, confirming, modifying or annulling the order appealed against. In terms of Sub-section (2) of Section 6C, if the appeal has been decided in favour of appellant, he is entitled to the possession of the confiscated goods and if

it is not possible for any reason to return the essential commodity seized from him, such person shall be paid the price therefor as if the essential commodity had been sold to the Government with reasonable interest calculated from the day of seizure of essential commodity and such price shall be determined in accordance with: (i) Sub-section (3B) of Section 3 in case of foodgrains, edible oils and oilseeds; (ii) Sub-section (3C) of Section 3 in case of sugar; and (iii) Sub-section (3) of Section 3 in case of any other essential commodity.

### **Confiscation and punishment**

Section 6D provides that the award of any confiscation under this Act by the Collector shall not prevent the infliction of any punishment to which the person affected thereby is liable under this Act.

### **Bar of Jurisdiction in Matters of Confiscation**

The 1976 Amendment Act has inserted Section 6-E in the Act which provides that no court, tribunal or authority shall have any jurisdiction to make an order with regard to the matters falling within the purview of this Act particularly wherever any essential commodity is seized in pursuance of an order made under Section 3 when the collector or the judicial authority appointed under Section 6C shall have the jurisdiction.

## **OFFENCES AND PENALTIES**

### **Cognizance of offences**

Section 10A of the Act declares that notwithstanding anything contained in the Criminal Procedure Code, 1971, every offence punishable under the Act shall be cognizable.

A cognizable offence is one, where, under the Criminal Procedure Code or any other law in force, a police officer may arrest a person without a warrant.

Section 11 lays down that before a Court can take cognizance of any offence punishable under the Act, the following three conditions must be satisfied, viz. (i) there must be a report in writing, (ii) the report must be made by a public servant, as defined in Section 21 of Indian Penal Code, or any aggrieved person or any recognised consumer association.

### **Prosecution of Public Servants (Section 15A)**

If any public servant is accused of any offence alleged to have been committed by him while acting, or purporting to act, in the discharge of his duties, in pursuance of any order made under Section 3, no court can take cognizance of such an offence except with the previous sanction—(a) of the Central Government in the case of a person who is employed in connection with the affairs of the Union; and (b) of the State Government in the case of a person who is employed in connection with the affairs of the State.

### **Penalties**

Section 7 of the Act deals with penalties. Contravention of an order passed by the Central Government under Section 3 with reference to clause (h) or (i) of Sub-section (2) thereof is punishable with imprisonment for a term which may extend to one year and also with fine [Section 7(1)(a)(i)]. For the contravention of an order with reference to other clauses of Sub-section (2) of Section 3 the punishment is imprisonment for a term ranging from three months to seven years and in addition fine is also leviable.

Further if any person contravenes any order made under Section 3, any property in respect of which the order has been contravened shall be forfeited to the Government and any package, covering, receptacle in which the property is found and any animal, vehicle, vessel or other conveyance used in carrying the property, could also be forfeited if the court so orders.

If any person to whom a direction is given under Section 3(4) (b) fails to comply with it, he shall be punishable with imprisonment for a term which shall not be less than three months but which may extend to seven years and shall also be liable to fine.

If any person convicted of an offence under Section 7(1)(a)(ii) or 7(2) is again convicted of an offence under the same provision he shall be punishable with imprisonment for the second and for every subsequent offence for a term which shall not be less than six months but which may extend to seven years besides fine. For adequate and sufficient reasons the court can award imprisonment for a term less than six months. Where an offence is committed for a second time, besides the above punishment, the Court can also order that the person shall not carry on any business of that essential commodity for such period not being\*less than six months as may be specified by the Court.



#### ***Mens rea (Sections 6A and 7)***

*In Nathulal v. State of Madhya Pradesh (AIR 1966 S.C. 43) it was held by the Supreme Court that mens rea or guilty mind is an ingredient of the offence punishable under Section 7 of the Essential Commodities Act, 1955 i.e., an intentional contravention of an order made under Section 3, is an essential ingredient of an offence under Section 7. In other words, if the dealer did believe bona fide that he could store the foodgrains for instance, without infringing any order under Section 3, there could be no contravention under Section 7.*

*It was observed by the Supreme Court in this case that mens rea is an essential ingredient of any criminal offence. Mens rea by necessary implication may be excluded from a statute only where it is absolutely clear that the implementation of the object of the Statute would otherwise be defeated. The nature of mens rea that would be implied in a Statute creating an offence depends on the object of the Act and the provisions thereof.*

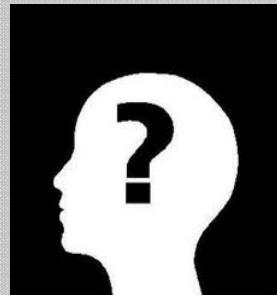
*In Hariprasad Rao v. State (AIR 1951 SC 264), it was observed that unless a Statute either clearly or by necessary implication rules out mens rea as a constituent part of a crime, an accused cannot be found guilty of an offence against the criminal law unless he has got a guilty mind. Therefore, mens rea is an essential ingredient of an offence under Section 7 of the Act.*

It is to be noted that the contravention under Section 6A is also of the same character. Section 6A in brief provides for seizure and confiscation based on 'contravention' of an order under Section 3. Therefore, the Collector before exercising his powers under the section would be entitled to take into consideration the question whether there was an intentional contravention of the order or whether the conduct of the dealer was bona fide under the belief that he was acting legally. But it should be remembered that the orders of the Collector are provisional in the sense that the Court is entitled, on appeal by the dealer, to look into whole matter to see whether there were reasons to confiscate the goods under Section 6A. It can be concluded that the provisions as regard 'contravention' under Section 6A or 7 are in pari materia—the contravention which details confiscation is of the same kind as that for which a dealer can be punished.

An interesting question is whether the doctrine of mens rea applies to cases of vicarious liability, as for instance, in the case of a master and servant. It is well accepted that the legislature cannot introduce the principles of vicarious liability and make the master liable for the act of his servants, although the master himself had no mens rea. Thus, in one case the charge against the respondents was that they sold some cloth in excess of the controlled price, and thus contravened the provisions of the Madhya Bharat Cotton Control Order; one of the respondents, Gangaram Saboo was not present in the shop at the time the cloth was alleged to have been sold, and it was, therefore, held that he could not be held vicariously liable for the act of his munim who had actually sold the cloth (*State v. Gangaram AIR 1935 H.B. 244*).

### Culpable Mental State

**Section 10-C provides for a presumption of culpable mental state, which includes intention, motive, knowledge of a fact and the belief in a fact. It is now provided that in any prosecution for an offence under the Act which requires a culpable mental state on the part of the accused, the Court shall presume the existence of mental state. Of course, it is open to the accused to prove that he had no such mental state with respect of the act committed by him.**



### Attempt and Abetment

Section 8 provides that any person who attempts to contravene or abets a contravention of any order made under Section 3 shall be deemed to have contravened that order.

### False Statement

A person shall be punishable under Section 9 with imprisonment for a term of which may extend to five years or with fine or with both for the following offences:

- (i) when required by any order made under Section 3 to make any statement or furnish any information, makes any statement or furnishes any information which is false in any material particular which he knows or has reasonable cause to believe to be false or does not believe to be true, or
- (ii) makes any such statement as aforesaid in any book, account, record, declaration, return or other document which he is required by any such order to maintain or furnish.

### Offences by Companies

Section 10(1) provides that if the person contravening an order under Section 3 is, a company, every person who, at the time of the contravention, was in charge of, and was responsible to, the company for the conduct of the business of the company, shall be deemed to be guilty of the contravention, and shall be liable to be punished accordingly. In such cases, the company itself is also liable to be proceeded against. Any such person, can, however, escape liability if he proves that the contravention took place without his knowledge, or that he exercised all due diligence to prevent it.

It may be noted that the term 'company' as used above, refers to any body corporate, and even includes a firm or other association or individuals. In the case of a firm, the term 'Director' would mean a partner in the firm.

### Publication of names of convicted companies by Court

Section 10-B of the Act provides that the Court may cause to be published in newspapers or in other manner at the expense of the company the name, place of business and the offence/contravention committed by it when a company has been convicted. However, no publication shall be made until the period for preferring an appeal against the order of the Court has expired, without any appeal having been preferred or where such appeal having been preferred, was disposed of. The expenses of any publication shall be recoverable from the company as if it were a fine imposed by Court.

### GRANT OF INJUNCTION BY CIVIL COURTS (SECTION 12B)

It is expressly provided by Section 12B that no Civil Court can grant any injunction or make any order for any other relief against the Central or State Government or any public officer, in respect of any act done, or purporting to be done, by such person in his official capacity under the Act, or any Order made thereunder, until after notice of the application for such injunction or other report is given to the Government or to such officer.

## **LESSON ROUND-UP**

- Essential Commodities Act, 1955 has been enacted to provide in the interest of the general public for the control of the production, supply and distribution of, and trade and commerce in, certain commodities.
- Section 2A dealing with Essential commodities declaration, etc. defines the "essential commodity" as to means a commodity specified in the Schedule to the Act.
- Central Government has been empowered to administer the provisions of the Act by issuing orders/directions notified in the official gazette and by delegating the authority to State Governments and administrators of Union Territories.
- An essential commodity which has been seized could be confiscated. Therefore, confiscation is an action posterior to the seizure of the essential commodity. A commodity that has not been seized cannot be confiscated. Seizure itself does not imply confiscation.
- *Mens rea* or guilty mind is an essential ingredient of the offence punishable under the Act.
- Culpable mental state, which includes intention, motive, knowledge of a fact and the belief in a fact.
- Where an offence is committed by a company, if it is proved that the offence had been committed with the consent or connivance of or is attributable to any neglect on the part of any Director, Manager, Secretary or other officer of the company, such a person shall be deemed to be guilty of that offence, and is liable to be proceeded against and punished accordingly.
- The Act expressly provides that no Civil Court can grant any injunction or make any order for any other relief against the Central or State Government or any public officer, in respect of any act done, or purporting to be done, by such person in his official capacity under the Act, or any Order made thereunder, until after notice of the application for such injunction or other report is given to the Government or to such officer.

## **SELF-TEST QUESTIONS**

1. What do you understand by essential commodities? What are the commodities termed as essential commodities, under the Essential Commodities Act?
2. Specify the authority responsible for the administration and execution of the Act ?
3. What do you know about an 'order' under the Act? What are the powers of Central Government in issuing the order under the Act?
4. There is difference in seizure and confiscation of commodities under the Act. How can the sale proceeds of confiscated commodities be utilized ? What is the procedure for disposal of confiscated goods?
5. A reasonable opportunity is required to be given to the person concerned before confiscation of his commodities or vehicle, etc., under the Act. Elaborate this statement in the light of provisions of the Act.

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# LAW RELATING TO ESSENTIAL COMODITIES, WEIGHTS AND MEASURES (THE LEGAL METEROLOGY ACT, 2009)

## Section II

### LESSON OUTLINE

- Legal Metrology
- International Organisation of Legal Metrology
- Standard Weight and Measure
- Appointment and powers of Director and Legal Metrology Officer
- Verification and Stamping of Weight and Measure
- Maintain Records and Registers
- Pre-packed Commodities
- Declaration on Pre-packed commodities
- Offences and penalties
- Forfeiture
- Power of the Central Government to make Rules
- Power of the State Government to make Rules
- Compounding offence
- Penalty for counterfeiting
- Offences by companies

### LEARNING OBJECTIVES

"Weights and measures may be ranked among the necessities of life to every individual of human society. They enter into the economical arrangements and daily concerns of every family", said *Mr. John Quincy Adams, the Sixth US President in his report to Congress in 1821*.

The essence of these words show the importance of weights and measures. In fact, the influence and impact of the system of weights and measures for trade use is as pervasive as ever. Weights and measures embrace every aspect of modern living. It is therefore critical for any country to have an accurate system of weights and measures. Such a system is indispensable in facilitating trade – as it fosters certainty, trust and confidence in all transactions involving weights and measures. It underpins fair trade and competition, and promotes efficiency, and in so doing, helps economy to grow.

Metrology studies many types of measurements. It studies not only length but also such measurements as weight and time. Each and every one of these elements can be studied in various manners as well. In metrology, there are set standards that are set for measurement qualities to determine what the typical measurement is. In many cases, they also have a well thought out plan as to how much of a degree of error there is as well in each measurement. There are various answers to questions about metrology because, in many cases, each theory can be right. Metrology goes back thousands of years to early civilization and was present well before the aspects of science as well.

The branch of knowledge concerning weights and measures is technically known as legal metrology. In basic form, metrology is the science of measurement.

Legal metrology Act, 2009 intend to establish and enforce standards of weights and measures, regulate trade and commerce in weights, measures and other goods which are sold or distributed by weight, measure or number and for matters connected therewith or incidental thereto.

## INTRODUCTION

*Legal Metrology* is the name by which the law relating to weights and measures is known in international parlance. Legal Metrology is very vital for scientific, technological and industrial progress of any country. The establishment of national standards of weights and measures and their proper enforcement aim at ensuring accuracy of measurements and measuring instruments and thus legal metrology strengthens the national economy in a broader sense besides being a potential instrument of consumer protection. The scope of legal metrology according to international practice extends to three broad fields of human activities, namely, commercial transactions, industrial measurements and measurements needed to ensure public health and human safety. The coverage of legal metrology varies from country to country. In some, almost all practical measurements are brought under the purview of legal metrology, whereas in other countries legal metrology finds restricted application in a few quantities like mass, length and volume used in trade and commerce. In most of the countries, however, legal metrology encompasses measurements which have a bearing on the protection of individuals from the financial and environmental points of view.

Legal metrology can be defined as that part of metrology which deals with units of measurement, methods of measurement and measuring instruments in so far as they concern statutory, technical and legal requirements which have the ultimate object of assuring public guarantee from the point of view of security and of appropriate accuracy of measurements.

## International Organization of Legal Metrology (OIML)

The International Organization of Legal Metrology (OIML) is an intergovernmental treaty organization whose membership includes Member States, countries which participate actively in technical activities, and Corresponding Members, countries which join the OIML as observers. It was established in 1955 in order to promote the global harmonization of legal metrology procedures. Since that time, the OIML has developed a worldwide technical structure that provides its Members with metrological guidelines for the elaboration of national and regional requirements concerning the manufacture and use of measuring instruments for legal metrology applications.

According to OIML legal Metrology is the entirety of the legislative, administrative and technical procedures established by, or by reference to public authorities, and implemented on their behalf in order to specify and to ensure, in a regulatory or contractual manner, the appropriate quality and credibility of measurements related to official controls, trade, health, safety and the environment.

The OIML develops model regulations, International Recommendations, which provide Members with an internationally agreed-upon basis for the establishment of national legislation on various categories of measuring instruments. Given the increasing national implementation of OIML guidelines, more and more manufacturers are referring to OIML International and Recommendations to ensure that their products meet international specifications for metrological performance and testing.

## OIML Certificate System for Measuring Instruments

The OIML Certificate System for Measuring Instruments was introduced in 1991 to facilitate administrative procedures and lower the costs associated with the international trade of measuring instruments subject to legal requirements. The System provides the possibility for a manufacturer to obtain an OIML Certificate and a Test Report indicating that a given instrument type (pattern) complies with the requirements of the relevant OIML International Recommendations. Certificates are delivered by OIML Member States that have established one or several Issuing Authorities responsible for processing applications by manufacturers wishing to have their instrument types (patterns) certified.

Certificates issued by OIML are accepted by national metrology services on a voluntary basis, and as the climate for mutual confidence and recognition of test results develops between OIML Members, the System serves to simplify the type (pattern) approval process for manufacturers and metrology authorities by eliminating costly duplication of application and test procedures.

## DEFINITIONS

Section 2 contains definitions of various terms used in the Legal Metrology Act. Some of the important ones are reproduced hereunder.

### Dealer

According to section 2(b) Dealer in relation to any weight or measure, means a person who, carries on, directly or otherwise, the business of buying, selling, supplying or distributing any such weight or measure, whether for cash or for deferred payment or for commission, remuneration or other valuable consideration; and includes a commission agent, an importer, a manufacturer, who sells, supplies, distributes or otherwise delivers any weight or measure manufactured by him to any person other than a dealer;

### Export

According to section 2(d)"export" with its grammatical variations and cognate expressions, means taking out of India to a place 'outside India;

### Import

According section 2(e) "import" with its grammatical variations and cognate expressions, means bringing into India from a place outside India;

### Label

Under clause (j) of section 2 "label" means any written, marked, stamped, printed or graphic matter affixed to, or appearing upon any pre-packaged commodity;

### Legal Metrology

As per section 2(g) "Legal Metrology" means that part of metrology which treats units of weighment and measurement, methods of weighment and measurement and weighing and measuring instruments, in relation to the mandatory technical and legal requirements which have the object of ensuring public guarantee from the point of view of security and accuracy of the weighments and measurements;

### Manufacture

As per section 2(i) "manufacturer" in relation to any weight or measure, means a person who -

- (i) manufactures weight or measure,
- (ii) manufactures one or more parts, and acquires other parts, of such weight or measure and, after assembling those parts, claims the end product to be a weight or measure manufactured by himself or itself, as the case may be,
- (iii) does not manufacture any part of such weight or measure but assembles parts thereof manufactured by others and claims the end product to be a weight or measure manufactured by himself or itself, as the case may be,
- (iv) puts, or causes to be put, his own mark on any complete weight or measure made or manufactured

by any other person and claims such product to be a weight or measure made or manufactured by himself or itself, as the case may be;

### **Protection**

Section 2"(k) define "protection" as to mean the utilisation of reading obtained from any weight or measure, for the purpose of determining any step which is required to be taken to safeguard the well-being of any human being or animal, or to protect any commodity, vegetation or thing, whether individually or collectively;

### **Pre-packed Commodity**

Section 2 (l) define "pre-packaged commodity" as to mean a commodity which without the purchaser being present is placed in a package of whatever nature, whether sealed or not, so that the product contained therein has a pre-determined quantity;

### **Person**

As per section 2(m) the term "person" includes,-

- (i) a Hindu undivided family,
- (ii) every department or office,
- (iii) every organisation established or constituted by Government,
- (iv) every local authority within the territory of India,
- (v) a company, firm and association of individuals,
- (vi) trust constituted under an Act,
- (vii) every co-operative society, constituted under an Act,
- (viii) every other society registered under the Societies Registration Act, 1860;

### **Premises**

As per section 2 (n) the term "premises" includes—

- (i) a place where any business, industry, production or transaction is carried on by a person, whether by himself or through an agent, by whatever name called, including the person who carries on the business in such premises,
- (ii) a warehouse, godown or other place where any weight or measure or other goods are stored or exhibited,
- (iii) a place where any books of account or other documents pertaining to any trade or transaction are kept,
- (iv) a dwelling house, if any part thereof is used for the purpose of carrying on any business, industry, production or trade,
- (v) a vehicle or vessel or any other mobile device, with the help of which any transaction or business is carried on;

### **Repairer**

Section 2 (P) defines "repairer" as to mean a person who repairs a weight or measure and includes a person who adjusts, cleans, lubricates or paints any weight or measure or renders any other service to such weight

or measure to ensure that such weight or measure conforms to the standards established by or under this Act;

### **Sale**

"Sale", with its grammatical variations and cognate expressions, means transfer of property in any weight, measure or other goods by one person to another for cash or for deferred payment or for any other valuable consideration and includes a transfer of any weight, measure or other goods on the hire-purchase system or any other system of payment by instalments, but does not include a mortgage or hypothecation of, or a charge or pledge on, such weight, measure or other goods;[section 2 (r)]

### **Seal**

As per section 2(s) "seal" means a device or process by which a stamp is made, and includes any wire or other accessory which is used for ensuring the integrity of any stamp;

### **Stamp**

Section 2(t) defines "stamp" as to mean a mark, made by impressing, casting, engraving, etching, branding, affixing pre-stressed paper seal or any other process in relation to, any weight or measure with a view to-

- (i) certifying that such weight or measure conforms to the standard specified by or under this Act, or
- (ii) indicating that any mark which was previously made thereon certifying that such weight Or measure conforms to the standards specified by or under this Act, has been obliterated;

### **Transaction**

Under section 2(u) "transaction" means,-

- (i) any contract, whether for sale, purchase, exchange or any other purpose, or
- (ii) any assessment of royalty, toll, duty or other dues, or
- (iii) the assessment of any work done, wages due or services rendered;

### **Verification**

As per section 2(v) "verification", with its grammatical variations and cognate expressions, includes, in relation to any weight or measure, the process of comparing, checking, testing or adjusting such weight or measure with a view to ensuring that such weight or measure conforms to the standards established by or under this Act and also includes re-verification and calibration;

### **Weight and measure**

Under section 2(w) "weight or measure" means a weight or measure specified by or under this Act and includes a weighing or measuring instrument.

## **STANDARD WEIGHTS AND MEASURES**

Chapter II of the Act containing sections 4 to 12 deals with standard weight and measure. Section 4 provides units of weights and measures to be based on metric system. Section 5 provides the base unit of weights and measures. Section 6 deals with base unit of numeration. Section 7 provides the standard units of weights and measures. Section 8 states standard weight, measure or numeral. Section 9 provides the reference, secondary and working standard. 10 deals with use of weight or measure for particular purposes. Section 11 contains prohibition of quotation, etc., otherwise than in terms of standard units of weight, measure or remuneration.

Section 4 of the Act provides that every unit of weight or measure shall be in accordance with the metric system based on the international system of units.

Section 5 of the Act provides that the base unit of length shall be the metre; mass shall be the kilogram; time shall be the second; electric current shall be the ampere; thermodynamic temperature shall be the kelvin; luminous intensity shall be the candela; and amount of substance shall be the mole.

Section 6 states that the base unit of numeration shall be the unit of the international form of Indian numeral. Every numeration shall be made in accordance with the decimal system. The decimal multiples and sub-multiples of the numerals shall be of such denominations and be written in such manner as may be prescribed.

As per section 7 of the Act the base units of weights and measures specified in section 5 shall be the standard units of weights and measures. The base unit of numeration specified in section 6 shall be the standard unit of numeration. For the purpose of deriving the value of base, derived and other units mentioned in section 5, the Central Government shall prepare or cause to be prepared objects or equipments in such manner as may be prescribed. The physical characteristics, configuration, constructional details, materials, equipments, performance, tolerances, period of re-verification, methods or procedures of tests shall be such as may be prescribed.

Section 8 provides that any weight or measure which conforms to the standard unit of such weight or measure and also conforms to such of the provisions of section 7 as are applicable to it shall be the standard weight or measure. Any numeral which conforms to the provisions of section 6 shall be the standard numeral.

No weight, measure or numeral, other than the standard weight, measure or numeral, shall be used as a standard weight, measure or numeral. No weight or measure, shall be manufactured or imported unless it conforms to the standards of weight or measure specified under section 8.

However, the aforesaid provisions shall not apply for manufacture done exclusively for export or for the purpose of any scientific investigation or research.

Section 11 of the Act provides that no person shall, in relation to any goods, things or service, quote, or make announcement of, whether by word of mouth or otherwise, any price or charge, or issue or exhibit any price list, invoice, cash memo or other document, or prepare or publish any advertisement, poster or other document, or indicate the net quantity of a pre-packaged commodity, or express in relation to any transaction or protection, any quantity or dimension, otherwise than in accordance with the standard unit of weight, measure or numeration.

It may be noted that the provisions mentioned above shall not be applicable for export of any goods, things or service.

Section 12 provides that any custom, usage, practice or method of whatever nature which permits a person to demand, receive or cause to be demanded or received, any quantity of article, thing or service in excess of or less than, the quantity specified by weight, measure or number in the contract or other agreement in relation to the said article, thing or service, shall be void.

### **Appointment and Power of Director, Controller and legal metrology officers**

Chapter III of the Act containing sections 13 to 23 of the Act deals with appointment and powers of director, controller and legal metrology officers.

Section 13 of the Act empowers the Central Government to appoint (by Notification) a Director of legal metrology, Additional Director, Joint Director, Deputy Director, Assistant Director and other employees for exercising the powers and discharging the duties conferred or imposed on them by or under this Act in relation to inter-State trade and commerce.

The Director and every legal metrology officer, appointed, shall exercise such powers and discharge such functions in respect of such local limits as the Central Government may, by notification, specify. Every legal metrology officer shall exercise powers and discharge duties under the general superintendence, direction and control of the Director.

The Director, the Controller and every legal metrology officer authorised to perform any duty by or under this Act shall be deemed to be a public servant within the meaning of section 21 of the Indian Penal Code. No suit, prosecution or other legal proceeding shall lie against the Director, the Controller and legal metrology officer authorised to perform any duty by or under this Act in respect of anything which is in good faith done or intended to be done under this Act or any rule or order made thereunder.

The Central Government may, with the consent of the State Government and subject to such conditions, limitations and restrictions as it may specify in this behalf, delegate such of the powers of the Director under this Act as it may think fit to the Controller of legal metrology in the State, and such Controller may, if he is of opinion that it is necessary or expedient in the public interest so to do, delegate such of the powers delegated to him as he may think fit to any legal metrology officer and where any such delegation of powers is made by such Controller, the person to whom such powers are delegated shall exercise those powers in the same manner and with the same effect as if they had been conferred on him directly by this Act and not by way of delegation.

Section 14 of the Act, provides that the State Government may, by notification, appoint a Controller of legal metrology, Additional Controller, Joint Controller, Deputy Controller, Assistant Controller, Inspector and other employees for the State for exercising the powers and discharging the duties conferred or imposed on them by or under this Act in relation to intra State trade and commerce.

The Controller and every legal metrology officer so appointed shall exercise such powers and discharge such functions in respect of such local limits as the State Government may, by notification, specify. Every legal metrology officer shall exercise and discharge the duties under the general superintendence, direction and control of the Controller.

### **Power of inspection, seizure**

Section 15 of the Act confer powers of inspection on the Director, Controller or any legal metrology officer may, if he has any reason to believe, whether from any information given to him by any person and taken down in writing or from personal knowledge or otherwise, that any weight or measure or other goods in relation to which any trade and commerce has taken place or is intended to take place and in respect of which an offence punishable under this Act appears to have been, or is likely to be, committed are either kept or concealed in any premises or are in the course of transportation.

The powers include entry at any reasonable time into any such premises and search for and inspect any weight, measure or other goods in relation to which trade and commerce has taken place, or is intended to take place and any record," register or other document relating thereto. The power also include seizer of any weight, measure or other goods and any record, register or other document or article which he has reason to believe may furnish evidence indicating that an offence punishable under the Act has been, or is likely to be, committed in the course of or in relation to, any trade and commerce.

Where any goods seized are subject to speedy or natural decay, the Director, Controller or legal metrology officer may dispose of such goods in such manner as may be prescribed. Every search or seizure made under this section shall be carried out in accordance with the provisions of the Code of Criminal Procedure, 1973, relating to searches and seizures.

### Forfeiture

Every non-standard or unverified weight or measure, and every package used in the course of, or in relation to, any trade and commerce and seized under section 15, shall be liable to be forfeited to the State Government.

However, such unverified weight or measure shall not be forfeited to the State Government if the person from whom such weight or measure was seized gets the same verified and stamped within such time as may be prescribed. Every weight, measure or other goods seized under section 15 but not forfeited shall be disposed of by such authority and in such manner as may be prescribed.

### Manufacturers. etc., to maintain records and registers

Section 17 of the Act provides that every manufacturer, repairer or dealer of weight or measure shall maintain such records and registers as may be prescribed. The records and registers maintained shall be produced at the time of inspection to the persons authorised for the purpose of Inspection.

#### ***Declarations on pre-packaged commodities***



*Section 18 states that no person shall manufacture, pack, sell, import, distribute, deliver, offer, expose or possess for sale any pre-packaged commodity unless such package is in such standard quantities or number and bears thereon such declarations and particulars in such manner as may be prescribed. Any advertisement mentioning the retail sale price of a pre-packaged commodity shall contain a declaration as to the net quantity or number of the commodity contained in the package in such form and manner as may be prescribed.*

### Registration for importer of weight or measure

Section 19 provides that no person shall import any weight or measure unless he is registered with the Director in such manner and on payment of such fees, as may be prescribed. No weight or measure, whether singly or as a part or component of any machine shall be imported unless it conforms to the standards of weight or measure established by or under this Act (Section 20).

### Approval of model

Every person, before manufacturing or importing any weight or measure shall seek the approval of model of such weight or measure in such manner, on payment of such fee and from such authority as may be prescribed. However, such approval of model may not be required in respect of any cast iron, brass, bullion, or carat weight or any beam scale, length measures (not being measuring tapes) which are ordinarily used in retail trade for measuring textiles or timber, capacity measures, not exceeding twenty litre in capacity, which are ordinarily used in retail trade for measuring kerosene, milk or potable liquors.

It may be noted that the prescribed authority may, if he is satisfied that the model of any weight or measure which has been approved in a country outside India conforms to the standards established by or under this Act, approve such model without any test or after such test as he may deem fit.

### **Prohibition manufacture, repair or sale of weight or measure without licence**

Section 23 of the Act provides that no person shall manufacture, repair or sell, or offer, expose or possess for repair or sale, any weight or measure unless he holds a licence issued by the Controller. However, no licence to repair shall be required by a manufacturer for repair of his own weight or measure in a State other than the State of manufacture of the same. The Controller shall issue a licence in such form and manner, on such conditions, for such period and such area of jurisdiction and on payment of such fee as may be prescribed.

Section 24 provides for verification and stamping of weight or, measure. Every person having any weight or measure in his possession, custody or control in circumstances indicating that such weight or measure is being, or is intended or is likely to be, used by him in any transaction or for protection, shall, before putting such weight or measure into such use, have such weight or measure verified at such place and during such hours as the Controller may, by general or special order, specify in this behalf, on payment of such fees as may be prescribed.

The Central Government may prescribe the kinds of weights and measures for which the verification is to be done through the Government approved Test Centre. The Government approved Test Centre shall be notified by the Central Government or the State Government, as the case may be, in such manner, on such terms and conditions and on payment of such fee as may be prescribed.

### **Offences and penalties**

Chapter V of the Act deals with offences and penalties.

Section 25 of the Act provides for penalty for use of non-standard Weight or measure. The section stipulates that whoever uses or keeps for use any weight or measure or makes use of any numeration otherwise than in accordance with the standards of weight or measure or the standard of numeration, as the case may be, specified by or under this Act, shall be punished with fine which may extend to twenty-five thousand rupees and for the second or subsequent offence, with imprisonment for a term which may extend to six months and also with fine.

Under section 26 Whoever tampers with, or alters in any way, any reference standard, secondary standard or working standard or increases or decreases or alters any weight or measure with a view to deceiving any person or knowing or having reason to believe that any person is likely to be deceived thereby, except where such alteration is made for the correction of any error noticed therein on verification, shall be punished with fine which may extend to fifty thousand rupees and for the second and subsequent offence with imprisonment for a term which shall not be less than six months but which may extend to one year or with fine or with both.

Section 27 provides that every person who manufactures or causes to be manufactured or sells or offers, exposes or possesses for sale, any weight or measure which, does not conform to the standards of weight or measure specified by or under this Act; or which bears thereon any inscription of weight, measure or number which does not conform to the standards of weight, measure or numeration specified by or under this Act, except where he is permitted to do so under this Act, shall be punished with a fine which may extend to twenty thousand rupees and for the second or subsequent offence with imprisonment for a term which may extend to three years or with fine or with both.

Section 30 dealing with penalty for transaction in contravention of standard weight or measure provides that whoever, in selling any article or thing by weight, measure or number, delivers or causes to be delivered to the purchaser any quantity or number of that article or thing less than the quantity or number contracted for

or paid for; or in rendering any service by weight, measure or number, renders that service less than the service contracted for or paid for; or in buying any article or thing by weight, measure or number, fraudulently receives, or causes to be received any quantity or number of that article or thing in excess of the quantity or number contracted for or paid for; or in obtaining any service by weight, measure or number, obtains that service in excess of the service contracted for or paid for, shall be punished with fine which may extend to ten thousand rupees, and; for the second or subsequent offence, with imprisonment for a term which may extend to one year, or with fine, or with both

Under section 31, Whoever, being required by or under this Act or the rules made thereunder to submit returns, maintain any record or register, or being required by the Director or the Controller or any legal metrology officer to produce before him for inspection any weight or measure or any document, register or other record relating thereto, omits or fails without any reasonable excuse, so to do, shall be punished with fine which may extend to five thousand rupees and for the second or subsequent offence, with imprisonment for a term which may extend to one year and also with fine.

Section 35 provides that whoever renders or causes to be rendered, any service through means other than the weight or measure or numeration or in terms of any weight, measure or number other than the standard weight or measure, shall be punished with fine which shall not be less than two thousand rupees but which may extend to five thousand rupees and for the second or subsequent offence, with imprisonment for a term which shall not be less than three months but which may extend to one year, or with fine, or with both.

Under section 36 Whoever manufactures, packs, imports, sells, distributes, delivers or otherwise transfers, offers, exposes or possesses for sale, or causes to be sold, distributed, delivered or otherwise transferred, offered, exposed for sale any pre-packaged commodity which does not conform to the declarations on the package as provided in this Act, shall be punished with fine which may extend to twenty-five thousand rupees, for the second offence, with fine which may extend to fifty thousand rupees and for the subsequent offence, with fine which shall not be less than fifty thousand rupees but which may extend to one lakh rupees or with imprisonment for a term which may extend to one year or with both. Whoever manufactures or packs or imports or causes to be manufactured or packed or imported, any pre-packaged commodity, with error in net quantity as may be prescribed shall be punished with fine which shall not be less than ten thousand rupees but which may extend to fifty thousand rupees and for the second and subsequent offence, with fine which may extend to one lakh rupees or with imprisonment for a term which may extend to one year or with both.

Section 42 provides for Vexatious search and empowers the Director, the Controller or any legal metrology officer, exercising powers under this Act or any rule made thereunder, who knows that there are no reasonable grounds for so doing, and yet searches, or causes to be searched, any house, conveyance or place; or searches any person; or seizes any weight; measure or other movable property shall, for every such offence, be punished with imprisonment for a term which may extend to one year, or with fine which may extend to ten thousand rupees or with both.

### **Penalty for counterfeiting or seals**

Section 44 provides that whoever counterfeits any seal specified by or under this Act or the rules made thereunder, or sells or otherwise disposes of any counterfeit seal, or possesses any counterfeit seal, or counterfeits or removes or tampers with any stamp, specified by or under this Act or rules made thereunder, or affixes the stamp so removed on, or inserts the same into, any other weight or measure, shall be punished with imprisonment for a term which shall not be less than six months but which may extend to one year and for the second or subsequent offence, with imprisonment for a term which shall not be less than six months but which may extend to five years.

"Counterfeit" shall have the meaning assigned to it in section 28 of the Indian Penal Code.



*A person is said to "counterfeit" who causes one thing to resemble another thing, intending by means of that resemblance to practice deception, or knowing it to be likely that deception will thereby be practiced.*

**Explanation 1.** It is not essential to counterfeiting that the imitation should be exact.

**Explanation 2.** When a person causes one thing to resemble another thing, and the resemblance is such that a person might be deceived thereby, it shall be presumed, until the contrary is proved, that the person so causing the one thing to resemble the other thing intended by means of that resemblance to practice deception or knew it to be likely that deception would thereby be practiced.

Whoever obtains, by unlawful means, any seal specified by or under this Act or the rules made thereunder and uses, or causes to be used, any such seal for making any stamp on any weight or measure with a view to representing that the stamp made by such seal is authorised by or under this Act or the rules made thereunder shall be punished with imprisonment for a term which shall not be less than six months but which may extend to one year and for the second or subsequent offence, with imprisonment for a term which shall not be less than six months but which may extend to five years.

Whoever, being in lawful possession of a seal specified by or under this Act or the rules made thereunder, uses, or causes to be used, such seal without any lawful authority for such use, shall be punished with imprisonment for a term which shall not be less than six months but which may extend to one year and for the second or subsequent offence, with imprisonment for a term which shall not be less than six months but which may extend to five years.

Whoever sells or offers or exposes for sale or otherwise disposes of any weight or measure which, he knows or has reason to believe, bears thereon a counterfeit stamp, shall be punished with imprisonment for a term which shall not be less than six months but which may extend to one year and for the second or subsequent offence, with imprisonment for a term which shall not be less than six months but which may extend to five years.

### Compounding of offence

In terms of offence punishable under section 25, sections 27 to 39, sections 45 to 47 either before or after the institution of the prosecution, be compounded, on payment for credit to the Government of such sum as may be prescribed.

However, the Director or legal metrology officer as may be specially authorised by him in this behalf, may compound offences punishable under section 25, sections 27 to 39, or any rule made under sub-section (3) of section 52. The Controller or legal metrology officer specially authorised by him, may compound offences punishable under section 25, sections 27 to 31, sections 33 to 37, sections 45 to 47, and any rule made under sub-section (3) of section 52:

Provided that such sum shall not, in any case, exceed the maximum amount of the fine, which may be imposed under this Act for the offence so compounded.

### Offences by companies

Section 49 provides that where an offence under this Act has been committed by a company, the person, if any, who has been nominated to be in charge of, and responsible to, the company for the conduct of the

business of the company (hereinafter in this section referred to as a person responsible); or where no person has been nominated, every person who at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company; and the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

However, such person shall not be liable to any punishment, if he proves that the offence was committed without his knowledge and that he exercised all due diligence to prevent the commission of such offence.

Any company may, by order in writing, authorise any of its directors to exercise all such powers and take all such steps as may be necessary or expedient to prevent the commission by the company of any offence under this Act and may give notice to the Director or the concerned Controller or any legal metrology officer authorised in this behalf by such Controller in such form and in such manner as may be prescribed, that it has nominated such director as the person responsible, along with the written consent of such director for being so nominated.

It may be noted that where a company has different establishments or branches or different, units in any establishment or branch, different persons may be nominated under this subsection in relation to different establishments or branches or units and the person nominated in relation to any establishment, branch or unit shall be deemed to be the person responsible in respect of such establishment, branch or unit.

Where an offence under the Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to the neglect on the part of, any director, manager, secretary or other officer, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Where any company is convicted under the Act for contravention of any of the provisions thereof, it shall be competent for the court convicting the company to cause the name and place of business of the company, nature of the contravention, the fact that the company has been so convicted and such other particulars as the court may consider to be appropriate in the circumstances of the case, to be published at the expense of the company in such newspaper or in such other manner as the court may direct. No publication shall be made until the period for preferring an appeal against the orders of the court has expired without any appeal having been preferred, or such an appeal, having been preferred, has been disposed of. The expenses of any publication shall be recoverable from the company as if it were a fine imposed by the court.'

***'Explanation.-***For the purposes of this section,-

- (a) "company" means any body corporate and includes a 'firm or other association of individuals; and
- (b) "director", in relation to a firm, means a partner in the firm but excludes nominated directors, honorary directors, Government nominated directors.

### **Power of the Central Government to make rules**

Section 52 of the Act empowers the Central Government to make rules, by notification, for carrying out the provisions of the Act.

In making any rule the Central Government may provide that a breach thereof shall be punishable with fine which may extend to five thousand rupees.

Every rule made by the Central Government under this Act 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 which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any

modification in the rule or both Houses agree that the rule should not be made, the rule shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule.

### Power of State Government to make rules

Section 53 empowers the State Government to make rules, by notification, and after consultation with the Central Government, to carry out the provisions of the Act.

In making any rule under this section, the State Government may provide that a breach thereof shall be punishable with fine which may extend to five thousand rupees. The power to make rules under this section shall be subject to the condition of the rules being made after previous publication in Official Gazette. Every rule made under this section shall, as soon as may be after it is made, be laid before each House of State Legislature, where there are two Houses and where there is one House of State Legislature, before that House.

### LESSON ROUND-UP

- Weights and measures may be ranked among the necessities of life to every individual of human society. They enter into the economical arrangements and daily concerns of every family.
- Legal metrology Act, 2009 intend to establish and enforce standards of weights and measures, regulate trade and commerce in weights, measures and other goods which are sold or distributed by weight, measure or number and for matters connected therewith or incidental thereto.
- "Legal Metrology" means that part of metrology which treats units of weighment and measurement, methods of weighment and measurement and weighing and measuring instruments, in relation to the mandatory technical and legal requirements which have the object of ensuring public guarantee from the point of view of security and accuracy of the weighments and measurements.
- Every unit of weight or measure to be in accordance with the metric system based on the international system of units.
- A person shall not manufacture, pack, sell, import, distribute, deliver, offer, expose or possess for sale any pre-packaged commodity unless such package is in such standard quantities or number and bears thereon such declarations and particulars in such manner as may be prescribed.
- Any advertisement mentioning the retail sale price of a pre-packaged commodity shall contain a declaration as to the net quantity or number of the commodity contained in the package in such form and manner as may be prescribed.
- Legal Metrology Act provides for penalty for use of non-standard Weight or measure.
- Label means any written, marked, stamped, printed or graphic matter affixed to, or appearing upon any pre-packaged commodity.
- A person is said to "counterfeit" who causes one thing to resemble another thing, intending by means of that resemblance to practice deception, or knowing it to be likely that deception will thereby be practiced.
- Legal Metrology Act empowers the Central Government and State Governments to make rules for carrying out the provisions of this Act.

## SELF-TEST QUESTIONS

1. What are the objectives of Legal Metrology Act, 2009?
  2. Enumerate the powers and functions of Controller and Legal Metrology Officer?
  3. Write short note on Counterfeit.
  4. Every non-standard weight and measure used in the course of trade is liable to be forfeited. Comment.
  5. Briefly explain the provision regarding declaration on pre-packed commodities.

# Lesson 11

## LAW RELATING TO SOCIETIES

### LESSON OUTLINE

- Introduction
- Registration of Society
- Procedure of Registration
- Rules and Regulation of Society
- Members — Their Rights and Liabilities
- When member is treated as strangers
- Property of the society
- Working and Management of Society
- Amendment and Alteration
- Suit by or against Society
- Amalgamation of Society
- Dissolution of the Society
- Consequence of Dissolution
- Registrar of Societies
- Offences and Penalties
- Enforcement of judgement against societies

### LEARNING OBJECTIVES

The concept of societies is not new to India. In ancient period, societies were the breeding ground for like-minded intellectuals to discuss important developments in the fields of arts, sciences, or for recreational purposes. In India, societies existed in the form of religious or charitable conventions dispensing relief to the needy.

Generally a need is felt to set up an institution of non-commercial nature for promotion of numerous charitable activities like education, art, religion, culture, music, social welfare, sports etc. Associations, clubs or societies are formed to help these purposes as they work on non-profit basis. To legalise such organisations, the Societies Registration Act, 1860 was enacted. The Societies Registration Act, 1860 is a pre-independence era legislation that envisaged the incorporation, management and dissolution of societies incorporated under the said Act.

For identical purposes, a non-profit association can be registered under Section 25 of the Companies Act, 1956. However, the registration, operation and management of an association registered under the Societies Registration Act, 1860 is easier and simpler comparatively. Therefore, it is essential for the students to be familiar with the law relating to Society.

According to the preamble, Societies Registration Act, 1860 is an Act for the Registration of Literary, Scientific and Charitable Societies. Whereas it is expedient the provision should be made for improving the legal condition of societies established for the promotion of literature, science, or the fine arts, or for the diffusion of useful knowledge, the diffusion of political education or for charitable purposes.

## INTRODUCTION

After the Constitution of India came into force, the Societies Registration Act 1860, (the main Act) has continued to be in force in all the States by virtue of Article 372 of the Constitution. A registered society is a legal entity but it is not a body corporate (*Board of Trustees v. State of Delhi* AIR 1962 SC 458). It is separate from its members. It can own properties. It is capable of suing or being sued. The position of a society is comparable with an incorporated company under the Companies Act 1956. Hence, a Company Secretary has an important role to play in registration and management of a registered society.

The main Act has been continuing to be applicable in all the States with some amendments made by almost all the States in operation, administration and management of societies within the respective States.

## Registration

A society can be registered by minimum seven individuals which may include foreigners, or registered society for the promotion of literature, science or fine arts or diffusion of useful knowledge and political education or charitable purposes, as specified in Section 20 of the main Act as under:-

- (i) Grant of charitable assistance.
- (ii) Creation of military orphan funds.
- (iii) Societies established at the several Presidencies of India.
- (iv) Promotion of –
  - Science
  - Literature
  - Fine Arts
  - Instructions or diffusion of useful knowledge
  - Diffusion of political education
  - Foundation or maintenance of libraries or reading rooms
  - Public museum and galleries of paintings
  - Works of art
  - Collections of natural history
  - Mechanical and philosophical investments
  - Instruments
  - Designs

Various States have added other objects like social welfare, sports & games, environment, compassion of living creatures, recreation, athletics, cultural activities, research work, welfare of physically handicapped etc.

A "charitable purpose" is a purpose which has some element of general public benefit; it does not embraces purposes which are religious or predominantly religious (*Md. Yunus v. The Inspector General of Registration* AIR 1980 Pat. 138). A charitable purpose includes religious purpose (*Hindu Public and another v. Rajdhani Puja Samithee and others* AIR 1999 SC 964).

## Procedure for Registration

The following documents are required to be filed with the Registrar of Societies for registration of a society under the main Act or corresponding Acts of various State Governments:-

1. Covering letter requesting for registration stating various documents annexed to it addressed to the

registering authority and signed by all the subscribers to the Memorandum or by a person authorised by all of them.

2. Memorandum of Association (in duplicate) containing (a) name of the society; (b) the objects of the society; (c) the names, addresses and occupation of the members of the governing body; (d) the place of registered office of the Society, and (e) the names, addresses and full signatures of the seven or more persons subscribing their names to the memorandum of Association. Their signatures should be witnessed.
3. Rules & Regulations/Bye-laws (in duplicate) duly signed by atleast three members of the governing body.
4. Affidavit on non-judicial stamp paper of requisite value by the President or secretary of the society duly attested by Oath Commissioner or Notary Public or Magistrate of first class.
5. Documentary proof such as rent receipt or property tax receipt in respect of the Registered office of the Society or no-objection of the owner of the premises.
6. Registration fee in cash or by demand draft.

The formalities and requirements may differ from State to State. Hence, it is advised that the applicant should contact the registering authority of the State in advance.

The Registering authority shall satisfy himself/herself about the compliance of the provisions of the Act and correctness of the documents and only thereafter certify in his/her hand that the Society is registered under the main Act or the corresponding Act of the State. On registration, the society becomes a legal entity or a judicial person apart from its members (*K.C. Thomas v. R.L. Gadeock AIR 1970 Pat. 160/163*). Its Rules & Regulations bound its members. It must confine its activities to the sphere embraced by its objects (*Ram Kumar v. State of West Bengal AIR 1953 Cal 534*). Any inconsistent object with the provisions of the applicable Act shall be inoperative even after registration (*Radhaswami Satsang Sabha Dayal Bag Vs. Hans Kumar Kishan Chand AIR 1959 MP 174*). A non-registered society may exist in fact but not in law. A unregistered society cannot claim benefits under the Income tax Act, 1961.

## Rules & Regulations

The Rules & Regulations help and guide the members and management of the society in carrying out its objects. They also bind members of the society. The Rules that are inconsistent with the provisions of the Act are inoperative although registered with the Registrar of Societies. The Rules & Regulations of a society may provide for—

- (i) the conditions of admissions of members,
- (ii) the liability of members for fines, forfeitures under certain circumstances,
- (iii) the consequence of non-payment of any subscription or fine registration and expulsion of members,
- (iv) the appointment and removal of trustees and their powers,
- (v) the manner of appointing and removing the governing body,
- (vi) the manner in which the notice of meetings may be given,
- (vii) the quorum necessary for the transactions of business at meetings of the society,
- (viii) the manner of making, altering and rescinding regulations,
- (ix) the investment of funds, keeping of accounts and for annual or periodical audit of account,

- (x) the manner of dissolving the society,
- (xi) the determination upon the dissolution that the property be utilised by the Government or others in particular manner,
- (xii) matters to be provided in bye-laws and the manner in which they shall be made,
- (xiii) such other matters as may be thought expedient having reference to the nature and objects of the society.

### **Society may make bye-laws**

A society can make its bye-laws in accordance with the Rules and Regulations of the society. If the rules do not provide for the making of bye-laws, bye-laws can be made at a general meeting of the society at which concurrent votes of three-fifths of the members present shall be necessary. If any penalty is imposed for the breach of any rule or bye-law of the society, such penalty can be recovered through the Court.

The bye-laws of a society may provide for:

- (a) The business hours of the society;
- (b) The objects of the society;
- (c) The activities of the society in furtherance of its objects;
- (d) The name of the person or officer, if any, authorised to sue or to be sued on behalf of the society;
- (e) The name of other person or officer who is empowered to give directions in regard to the business of the society;
- (f) Enrolment of members –
  - (i) Qualifications for membership, classification, restrictions and conditions, if any, therefor,
  - (ii) The entrance and other fee, or subscription, if any, to be collected from members,
  - (iii) The dates prescribed for payment of the amount specified in sub-clause (ii) above and levy of penalties or fine, if any, imposed on defaulting members.
- (g) Removal of members, the circumstances under which members could be removed from the rolls and the procedure for such removal and appeal, if any, against such removal;
- (h) Rights, applications, privileges of members;
- (i) The manner in which the society shall transact its business;
- (j) The constitution of the Committee and qualifications of the members of the Committee, their term of office and the procedure for their appointment and reappointment;
- (k) The preparation and filing with the concerned Registrar, of records, annual lists or other statements;
- (l) Audit of accounts and the balance-sheet for the financial year;
- (m) The supply of copies of bye-laws, the receipt and expenditure account and of the balance sheet to the members on application and the fee payable for the same;
- (n) Imposition of fine, if any, for breach of the provisions of the bye-laws by any member or officer;
- (o) The mode of custody, application and investment of the funds of the society and the extent and conditions of such investment;
- (p) Funds earmarked specifically for the purpose of making provisions for dependent of a deceased or disabled member and the quantum of payment to be made thereof;

- (q) Arrangements for transactions of day-to-day business of the society, the expenditure to be incurred therefor, the staff to be employed and condition of services of such employees;
- (r) (i) Conduct of annual general meetings and procedure therefor,
- (ii) Conduct of extraordinary general meetings and procedure therefor and the number of members required for making a requisition in writing, calling for such a meeting,
- (s) Exhibition of the Register of Members, the books containing minutes and the books of accounts at the registered office of the society during business hours for inspection by its members free of charge.

The bye-laws may also deal with such other matters incidental to the organisation and working of the society and the management of its business as may be deemed necessary.

### **Members — Their Rights and Liabilities**

A member means a person who has —

- (a) been admitted to the society according to its rules and regulations;
- (b) paid subscription provided in the rules;
- (c) signed the roll or list of members of the society, and
- (d) not resigned or ceased from the membership of the society.

Any arrear of subscription amount for a period of exceeding three months is disqualification for continuing to be a member and vote.

No one can claim admission to a society as a matter of right on payment of the prescribed subscription. The discretion of the governing body is final concerning grant or refusal of admission to a person [*Abhoy Pado Bose v. Queen's Anglo Sanskrit School, Lucknow* 34.1.C.263 (Oudh)].

#### **Choose the correct answer**

*Which of the following must be adhered to by a society while making its bye-laws?*

- (a) *The rules and regulations of the society*
- (b) *The shape and size of the society*
- (c) *The power and stability of the society*
- (d) *None of the above*

**Correct Answer:** a

### **When members treated as strangers?**

A member of the society is liable to be sued as stranger in the following cases:

- (i) When he is in arrear of a subscription which he is bound to pay according to the rules, or
- (ii) When he has detained any property of the society, or
- (iii) When he has destroyed any property of the society.

In above cases the member may be sued for such, arrears and damages. But he can recover the costs if he is successful in the suit (Section 10).

A member is subject to prosecution and punishment as stranger for committing the following offences:

If he (i) steals, or purloins, or embezzles any money or other property or (ii) willfully and maliciously destroy or injures any property of the Society or (iii) forges any deed, bond, security for money, receipt or other instrument whereby the funds of the Society may be recovered when accrued in any Court having jurisdiction where the defendant resides or the Society is situated, as is deemed expedient by the governing body (Section 11).

Members guilty of offences are punishable as strangers. A member of the society may be prosecuted for wilful and malicious destruction or injury to the property of the society or for forgery, exposing the funds of the society to loss.

The members of a society have rights to —

- receive notice of all special and annual general meetings;
- vote at all meetings.
- resolve all disputes among members and society or *inter se*;
- receive copies of the rules and regulations and bye-laws.

Their liabilities are —

- A member may be sued as a stranger by the society.
- Member, guilty of an offence to the society, is punishable as a stranger;
- Member causing breach of any rule or regulation or bye-law of the society is liable to pay penalty under the Bye-Laws.
- Member who is guilty of misfeasance or breach of trust or misapplication of funds in relation to the society shall be accountable to make good the loss so caused to the society.

### **Property of Society: Where it vests?**

Section 5 of the Act lays down the provisions for vesting of property of the Society. It is presumed that the property, both movable and immovable, belonging to the Society, vests in trustees. But if it is not vested in trustees, Section 6 provides that then it shall be deemed to be vested in the governing body of such Society for the time being. In all civil or criminal proceedings the property may be described as the property of the governing body of such society by their proper title.

The Act does not create in the members of the registered Society any interest other than that of the bare trustees. A property, which has vested in the trustees before registration of the Society, becomes as from, the registration of the Society, a property belonging to the Society and must be deemed to be the property of the Society. As a matter of fact there is no transfer of ownership that which belonged to a registered Society continues after the change in status of that Society on being registered, as belonging to the registered Society (AIR 1953 Cal. 140).

In the case of *Board of Trustee, Ayurvedic and Unani Tibbia College v. State of Delhi*, A.I.R. 1962, SC 458, the Board of Trustees of Tibbia College was dissolved by the Tibbia College in 1952 and the property which had vested in the Board of Trustees, passed to the newly constituted Board.

## Working and Management of Society

As the society is a legal person having no physical existence, its governing body is its brain. Its activities are managed, executed and supervised by the governing body. It has to work within the objects of the society in accordance with the rules, regulations and bye-laws and to carry out the statutory duties under the main Act or the corresponding State Act. The governing body shall also be constituted in accordance with the rules and regulations of the society. The property of the society vests in the governing body and not in the members. The filing and defending the suits by the society shall continue in the original form and the changes in the governing body shall not affect.

There should be minimum three members of the governing body. Its members are either elected or nominated as per the rules and regulations of the society. The term of office of members is three years and members can enjoy two terms. However, the term, retirement, expulsion are governed by the rules and regulations of the society.

The members of the governing body are the trustees of the properties of the society. They have to look after and manage the properties of the society. Here, property means both movable and immovable property. The properties of the society vest in the trustees and when there is no trustee, in the governing body. A trustee is a man who is the owner of the property and deals with it as principal owner and master subject only to an equitable obligation to account to some person to whom he stands in relation of trust and who is *cestric que trust*.

The members of governing body is collectively responsible and accountable to comply with the statutory provisions of the Act for carrying out the functions of the society to achieve its objective(s) for which it is set up. The duties are detailed hereunder:-

1. To hold annual general meeting as per the rules and regulations of the society for laying before such meeting the statement of activities, Income & Expenditure Account and other information as provided in the rules and regulations for the purpose;
2. A list of the names, addresses and occupations of the governors, council, directors, committee or other governing body to which the management of the society is entrusted, is to be filed with the Registrar or such authority as prescribed once in a year either within 14 days of the date of holding such meeting or in the month of January every year.
3. To hold extra-ordinary general meeting to transact some special business, which cannot be waited or delayed, till the holding of the annual general meeting. The purposes of such meeting may be to amend, alter or change in name or address or extensions of operation etc.
4. To report changes or alterations made in the managing, governing body or in the rules of the society to the Registrar.
5. To file notice of situation of the registered office of the society and of any change therein with the Registrar.
6. To register amendment in Memorandum of Association or Bye-laws with the Registrar by way of an application with a copy of the special resolution of the amendment with filing fee.
7. To supply copies of the Bye-laws, the Receipts/Incomes & Expenditure Account and Balance Sheet to the members of the society on their application with the fees, if any, prescribed by the society.
8. To invest and apply the funds and properties of the society in a manner as a prudent man will apply his own funds.

9. To keep and maintain a register of members of the society in accordance with the rules and regulations of the society.
10. To display the name of the society prominently at its registered office and other places of business.
11. To produce or submit periodical statement of Receipts Incomes & Expenditure A/c, Assets & Liabilities of the society.
12. To file a certified copy of every special resolution duly signed by an authorised officer of the society with the Registrar within the prescribed time.
13. To keep and maintain minutes of the meetings of the governing body and general body correctly and truly at the registered office of the society.
14. To retain all the important documents permanently.
15. To prepare periodical Accounts of the society and get them audited and to file Income-Tax Return, and
16. To attend all other duties as may be provided in the rules and regulations of the society.

### **Amendment or Alteration**

The objects of a society are its constitution and the society has to act within the framework of its objects. Any act done by the society beyond the objects clause shall be *ultra vires*. Under Section 12 of the main Act, the following steps are required for alteration, extension or abridgment of the objects of a society –

1. Submission of the proposal by the governing body to the members of the society;
2. Ten days notice to members about holding of a special general meeting;
3. Convening a special meeting for consideration and passing of the proposal by 3/5th of the members;
4. Convening second special general meeting after a month; and
5. Confirmation to the proposal by 3/5th of the members present at the second special meeting.

The above procedure is also required to be followed for alteration or amendment of the Rules and Regulations or Bye-laws, change of name, and change in the registered office. Every change is required to be registered with the Registrar or the authority as prescribed as per the rules and regulations of the society.

### **Suits by and against Society**

A Society registered under the Act is a legal entity. It is capable of suing and be sued in the name of the president, chairman or principal, secretary or trustees as determined by the rules and regulations. If there is no such prescribed determination then in the name of such person as appointed by the governing body for the occasion. If no such person is nominated by the governing body on an application made to it, then a person having a claim against society may sue the president or chairman or secretary or trustee.

No suit or proceeding in any Civil Court shall abate or discontinue if the person in whose name the suit has been brought has died or ceased to fill the character. Such suit shall be continued in the name of or against the successor of such person.

The section is merely an enabling provision and does not take away the right of society to sue or be sued in its own name (*Govind Prasad v. Laxminarain* 1960 MPLJ 145).

The provisions contained in Sections 6 and 7 are not mandatory. The words 'for the occasion' in Section 6 of the Act are significant whereas under the rules and regulations of a Society, a general authority can be

conferred on the chairman, secretary or trustee for suing or being sued on behalf of the Society. But an authority given by the governing body has to be limited to the 'occasion' concerned. The object is that registered Societies should not embark upon needless and endless litigations. They must at each distinct stage of the litigation (e.g. to file a suit, to file an appeal) decide whether to pursue the matter further or not etc.

In *Sonar Bangla Bank v. Calcutta Engineering College* (1960) Cal. 409, it was held that the provisions of Section 6 are not mandatory but permissive.

### **Enforcement of Judgement Against Society**

It is the property of the Society against whom the judgment is enforced although the judgment is named against the person or officer on behalf of the society. It will not be enforced against the person or officer or his property. The application for execution shall set forth the fact of the party against whom it shall have been recovered. Judgements recovered against the nominees of a society are enforceable against the property of the society and not against the property or bodies of those nominees.

### **Amalgamation or Division of the Society**

Under Section 12 of the main Act, a society may be amalgamated with any other society, either wholly or partially by the governing bodies of the societies for the better utilisation of the properties, resources or any other purpose. The procedure is mandatory (*Prasanna Venkatesa Ra v. K. Srinivasa Ra* 59 MLJ 770). The following actions are to be complied with —

1. Submission of the proposal of amalgamation by the governing body to the members of the society by a printed report;
2. Holding special general meeting by giving ten days notice to the members for consideration and passing resolution for the proposed amalgamation by 3/5th majority of the members, present thereat;
3. Convening another special general meeting after a month for confirmation to the first resolution passed at the first special general meeting by 3/5th majority of the members present thereat.

The majority of a body cannot alter the fundamental principles of the body unless such power is specially reserved. The Government may order division or amalgamation of a society after giving the society an opportunity to represent against such proposal.

### **Dissolution of Society**

Under Section 13 of the main Act, a society can be dissolved. Dissolution of a society becomes necessary where the objects for which it is formed, has been fulfilled or where the purposes for which it is formed, have become irrelevant, invalid or inoperative or by passing of a resolution by 3/5th majority of the members present at a meeting to dissolve the society for utilisation of its assets for some other better uses. A society may be dissolved forthwith or within the agreed time. The following steps are to be taken:—

1. Decision of the governing body;
2. Convene a special general meeting of the members by giving a requisite notice for consideration and passing resolution by 3/5th majority of the members present thereat;
3. Decision as to dissolve it forthwith or at a later time agreed upon by them.
4. Decision for the actions to be taken for disposal of properties and settlement of claims and liabilities as per the rules and regulations of the society; and
5. Delegate authority to the person(s) of the governing body to comply with the decisions accordingly.

Where any Government is a member of the society or has contributed the funds to the society or is otherwise interested therein, the society shall have to obtain prior consent of such Government for the purpose.

Where any dispute arises on dissolution of a society relating to adjustment of its affairs, it should be referred to the principle Court of the original civil jurisdiction of the District where the chief building of the society is situated. The District Civil Court has the jurisdiction to decide the dispute of a society.

The main Act does not provide for dissolution of societies by the Registrar. Various States, of course, have made provisions for dissolution by the Registrar under the following circumstances—

- (1) Where the office of the society has ceased to be in the State of registration, or
- (2) Where the society has shifted its office from the State of registration to some other State, or
- (3) Where the activities of the society are considered subversive, or
- (4) Where it is carrying on any unlawful activity, or
- (5) Where it has allowed any unlawful activity to be carried on within any premises under its control,
- (6) Where the registered society has contravened any of the provisions of the Act or the rules made thereunder, or
- (7) Where the registered society is insolvent or must necessarily become so, or
- (8) Where the business of such registered society is conducted fraudulently or not in accordance with the bye-laws or the objects specified in the memorandum of the society, or
- (9) Where the society contravened any provision of any other law for the time being in force, or
- (10) Where the number of members of the society is reduced below seven, or
- (11) Where the society has ceased to function for more than three years, or
- (12) Where the society is unable to pay its debts or meet its liability, or
- (13) Where the registration of the society has been cancelled on the ground that its activities or proposed activities have been or will be opposed to public policy.

The Registrar normally inquires or investigates into the activities of the society and calls upon the society to show cause why it should not be dissolved. The Registrar may move the Court for making an order for dissolution of the society, if the cause shown by the society is not satisfactory.

Similarly, the main Act does not provide for dissolution by the Court. But in some States, the Court may order for dissolution of a society on application by 10% of its members or the Registrar on having been satisfied that any one or more of the following circumstances exist:—

- (1) If there is any contravention by the society of the provisions of the Act, or
- (2) If the number of members is less than seven, or
- (3) If the society has ceased to function for more than three years, or
- (4) If the society is unable to pay its debts or meet its liabilities, or
- (5) If it is proper that the society has to be cancelled on the ground of its activities or
- (6) If proposed activities have been or will be opposed to the public policy.
- (7) If the activities of the society constitute a public nuisance,
- (8) If the activities of the society are otherwise opposed to public policy.

The Government may by written order containing detailed reasons, dissolve a society. Before passing such order an opportunity has to be given to the society for representation against dissolution. Any order of withdrawal of registration without notice or opportunity to the society for representation in the matter shall be against the rule of natural justice.

### Consequences of Dissolution

Dissolution of a society results in cessation of its activities. Its liabilities are to be settled suitably and its surplus assets are to be given to another society or the Government in terms of its rules and regulations. If the rules do not provide in the matter, the governing body of the society shall take appropriate steps with requisite majority vote or as directed by the Registrar or the Court. But in no circumstances, the surplus assets of the dissolved society can be paid or distributed amongst its members or any of them.

### Registrar of Societies — Powers & Duties

The main Act makes an indirect reference to the powers of the Registrar under Sections 1,2,3,4,17,18 and 19. Under the corresponding Acts of various States different powers and duties are given to the Registrar. These are —

1. Allow inspection of documents by any person and provide certified copy thereof on payment of fees as prescribed,
2. Call information, explanation or returns from the societies relating to the affairs, employees, documents filed, accounts etc,
3. Hold inquiries and settle disputes *suo moto* or at the request of the members of the governing body or other members,
4. Investigate into the affairs of the society,
5. Cancel registration on happening of certain events,
6. Refuse registration, if the name is undesirable or identical or the objects are contrary to any other law etc,
7. Order amendment of Memorandum of Association, rules and regulations, bye-laws of society,
8. Seize and take possession of the books and records, funds and property of the society,
9. Summon and enforce attendance of witness including the parties interested for giving evidence and producing documents,
10. Order for auditing of the accounts of the society,
11. Compounding offences on application with fee,
12. Settle disputes regarding election of the office bearers,
13. Restoration of the property or money of the society,
14. Removal of the defunct society from the register of societies,
15. Condonation of delay in filing of documents,
16. Appointing liquidator.

### Offences and Penalties

The main Act does not provide for any offences and penalties for breach or contravention of its provisions. However, various State Governments have amended the main Act to provide for offences and penalties for non-compliance. No Court inferior to that of a Magistrate of the first class shall try any offence punishable under the main Act. No Court shall take cognizance of any offence except upon complaint made by the Registrar of Societies or any authorised person by him.

## **LESSON ROUND-UP**

- A registered society is a legal entity but it is not a body corporate. It is separate from its members. It can own properties. It is capable of suing or being sued. The position of a society is comparable with an incorporated company under the Companies Act 1956.
- A society can be registered by minimum seven individuals which may include foreigners, or registered society for the promotion of literature, science or fine arts or diffusion of useful knowledge and political education or charitable purposes.
- The Rules & Regulations help and guide the members and management of the society in carrying out its objects. They also bind members of the society. The Rules that are inconsistent with the provisions of the Act are inoperative although registered with the Registrar of Societies.
- As the society is a legal person having no physical existence, its governing body is its brain. Its activities are managed, executed and supervised by the governing body. It has to work within the objects of the society in accordance with the rules, regulations and bye-laws and to carry out the statutory duties under the main Act or the corresponding State Act.
- A Society registered under the Act is a legal entity. It is capable of suing and be sued in the name of the president, chairman or principal, secretary or trustees as determined by the rules and regulations.
- Dissolution of a society becomes necessary where the objects for which it is formed, has been fulfilled or where the purposes for which it is formed, have become irrelevant, invalid or inoperative or by passing of a resolution by 3/5th majority of the members present at a meeting to dissolve the society for utilisation of its assets for some other better uses.

## **SELF-TEST QUESTIONS**

1. Discuss the status of a Society registered under the Act.
2. Briefly explain the procedure for formation and registration of Societies.
3. Who is a member of society?
4. What are the powers of a Society? How its' property vests?
5. Discuss briefly the dissolution of a Society.
6. Discuss the powers of a Society to alter its purposes.

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# Lesson 12

## LAW RELATING TO TRUST

### LESSON OUTLINE

- Introduction to Trust
- Scope of the Trust Act
- Trust and Contract
- Classification of Trust
- Simple and Special Trusts
- Oral and Written Trusts
- Charitable Trusts
- Religious Trusts
- Expressed and Implied Trust
- Public and Private Trust
- Creation of Trust
- Certainties of Trust
- Duties of Trustee
- Liabilities of Trustee
- Power of Trustee
- Disabilities of Trustees
- Beneficiary
- Doctrine of Cypres
- Extinction of Trust
- Revocation of Trust

### LEARNING OBJECTIVES

The concept of 'trust' relates to the ancient times. When the properties were dedicated for charitable, pious, religious, social welfare, educational, medical purposes. The Trust laws came to India via English Trust law which stipulates dual ownership of trust property i.e. legal title vests with the trustee while equitable title vests with the beneficiary. On this basis, Indian Trusts Act 1882 was enacted. The Indian Trusts Act, 1882 codifies the law relating to private trusts and private trustees under different subject heads which include Creation of trusts; Duties and liabilities of trustees; Their rights and powers; Their disabilities; The rights and liabilities of the beneficiary; Vacating the office of trustee; The extinction of trusts and; Certain obligations in the nature of trusts.

Hindu charitable or religious trusts are mainly governed by the provisions of Hindu Laws which have been passed by several States under Article 25 (2) of the Constitution of India, like, The Bombay Public Trust Act, 1950, Rajasthan Public Trust Act, 1959, Madras Hindu Religious and Charitable Endowment Act, 1959 etc. The Wakf Act 1995 regulates muslim Wakfs for public benefit. There are also several States laws for regulating the proper administration of Wakfs in India. There are other trust laws like, Sikh Gurdwara Act, 1925 governing Sikh Gurdwaras.

In this lesson, all issues relating to formation, types and other matters relating to trusts are discussed.

## INTRODUCTION

The concept of 'trust' relates to the ancient times. When the properties were dedicated for charitable, pious, religious, social welfare, educational, medical purposes. Now a days, it has gained a greater significance for various tax exemptions made available to a trust which is treated as a separate legal entity.

A 'trust' is an obligation annexed to the ownership of property and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another or of another and the owner.

The following are the essential elements of a trust :-

1. the author or the settler of the trust;
2. the trustee;
3. the beneficiary;
4. the trust property or the subject-matter of trust
5. the object of the trust;
6. the instrument of trust.

## Indian Trust Act

In view of a plethora of Trust laws, Indian Trust Act 1882 has been considered desirable to be discussed hereunder and for brevity it is referred hereinafter as "The Trust Act".

The Act is divided into the following parts:

- (i) preliminary;
- (ii) the creation of trusts;
- (iii) the duties and liabilities of trustees;
- (iv) their rights and powers;
- (v) their disabilities;
- (vi) the rights and liabilities of the beneficiary;
- (vii) vacating the office of trustee;
- (viii) the extinction of trusts; and
- (ix) certain obligations in the nature of trusts.

## Scope

As is clear from the preamble, the Act has no application to public or private, religious or charitable endowment.

The Indian Trusts Act is exhaustive in respect of any matter specifically provided for in it, but it is not exhaustive of all matters relating to private trusts. Therefore, in cases covered by the Act, its provisions must be applied but if a case is not covered by it, the Court is entitled to apply rules of English law, as laid down by judicial decisions in that country and which are not inconsistent with the Act, as the rules of justice, equity and good conscience.

**Choose the correct answer**

Which of the following is not an essential element of a trust?

- (a) The trustee
- (b) The beneficiary
- (c) The name of the trust
- (d) The instrument of trust

**Correct Answer: c**

**Definition of Trust**

The Act defines the term 'trust' in Section 3 as (i) an obligation annexed to the ownership of property and (ii) arising out of confidence reposed in and (iii) accepted by the owner or declared and accepted by him, (iv) for the benefit of another or of another and the owner.

The person who reposes or declares the confidence is called the 'author of the trusts', the person who accepts the confidence is called the 'trustee', the person for whose benefit the confidence is accepted is called the 'beneficiary'; the subject matter of the trust is called 'trust property' or 'trusts money'; the 'beneficial interest' is beneficiary's right against the trustee as owner of the trust property; and the instrument declaring the trust is called the 'instrument of trust'.

The word 'trust' in its legal sense has a technical and definite meaning which is very much different from the sense in which this word is used in daily parlance. Trust connotes a legal concept or relationship similarly as other relationships created by law, e.g., Contract, Agency.

**Trust and Contract**

Trust in its origin was a form of contract distinctively enforced in equity. A contract creates a trust where it has brought into existence an obligation annexed to the ownership of property for the benefit of a person other than the owner. No technical words are required to create a trust.

There is always a fiduciary relationship between trustee and beneficiary, but not between the parties to a contract.

**Difference Between Trust and Bailment, Trust and Agency**

The definition of Bailment is given in Section 148 of the Indian Contract Act, 1872. The following is the difference between a trust and a bailment.

- (i) A trustee becomes the full owner of trust property. A bailee acquires special property only.
- (ii) The obligation of the bailee is legal, whereas that of a trustee is equitable.
- (iii) A bailment may be created for movable property only. A trust may be created for both movable and immovable properties.

**Difference between Trust and Agency**

- (i) An agent has no title to the property. A trustee is the full owner of the trust property.
- (ii) An agent acts on behalf of his principal and is subject to his control. A trustee acts in his own right.
- (iii) An agent is generally not personally liable, a trustee is.

## CLASSIFICATION OF TRUSTS

Trusts are divisible into several classes according to the mode of their creation. Some of the important classes are as follows:

### Simple and Special Trusts

Where the trustee is merely to hold the estate without having any active duties to perform it is called a simple trust. Where, however, the trust has been created for a particular object or purpose there is a special trust. Thus, in a simple trust, the trustee is merely to hold the property for the benefit of the beneficiary and in a special trust, the trustee has duties to perform.

### Oral and Written Trusts

A trust may be declared either orally or through an instrument in writing. However, a trust in relation of movable property can be declared orally by transferring the possession of the property with a direction that the property be held in trust. In regard to a private trust for immovable properties, a written trust deed is prerequisite.

### Charitable or Religious Trust

In order to determine whether a deed of trust is a valid public or charitable trust, it is necessary to see what is the dominant intention of the testator, namely, who are the real objects of his bequest and secondly whether the class indicated as the object of charity forms at least a section of the public. Where the main and paramount intention of the settler was to benefit the members of his family and thereafter the members of his caste who might need assistance from such funds there could be no public or charitable trust created.

It is one of the cardinal rules governing execution of charitable trusts that the intention of the donor must be observed. This principle has been evolved as an auxiliary to this rule and is never allowed to defeat it. If the charity can be administered according to the directions of the founder, the law requires that it should be so administered. The Courts will not allow any departure from them on the grounds of expediency.

*Cy pres* means near to it. The doctrine of *Cy pres* applies only to charitable trusts. The reason is that a public charity is perpetual and the rule against perpetuity does not apply to it. It can never die though its nature may be changed. In *Halsbury's Law of England*, in 3rd Edn. Vol. 4, P. 317, it is stated:

"Where a clear charitable intention is expressed, it will not be permitted to fail because the mode, if specified, cannot be executed, but the law will substitute another mode *Cy pres*, that is, as near as possible to the mode specified by the 'donor'.

However, the above doctrine is subject to the doctrine of severability, i.e., the doctrine of *Cy pres*, applies if the nature of the charitable object is general and not specific.

### Express and Implied Trusts

Express trusts are created by the act of parties either in words or in writing. While an implied trust is one which is deduced from the conduct of the parties and the circumstances of the transactions.

### Public and Private Trusts

The criterion for deciding whether a particular trust is or is not of a private nature, is whether the said trust is or is not for the benefit of individuals. Where the intention of the founder, as shown by the recitals in his Will, was that the property was to be dedicated for the benefit of idols, the trust is undoubtedly of a public nature and not for the benefit of the individual members of family.

The essential difference between a private and a public trust is that in the former the beneficiaries are definite and ascertained individuals or individuals who within definite time can be definitely ascertained but in the latter the beneficial interest must be vested in an uncertain and fluctuating body of persons either the public at large or some considerable portion of it answering a particular description.

### Revocable and Irrevocable Trusts

A revocable trust is one which is revocable when it is created by a non-testamentary instrument or orally and a power of revocation has been expressly reserved by the settler. A trust may be revoked by the consent of all the beneficiaries who are competent to contract (Section 78).

All other trusts are irrevocable. Besides if a trust is created for charitable or religious purposes, such a trust cannot be revoked.

### Public-cum-Private Trust

A Public-cum-Private Trust is one in which a religious trust is created for the immovable property like a Temple, Durgah etc. in the nature of a public trust but there is a direction for use of income through offerings or otherwise for public purposes and also a part thereof to person(s) in charge of the Temple, Durgah etc. A public-cum-private trust may become a fully public trust when the private beneficiary(ies) renounces his/their rights to which they are entitled.

### Constructive Trust

A constructive trust is one which is not created by the express or implied act of the settler, but which is deemed by operation of law or arises by construction of law. A constructive trust is a relationship with respect to a property subjecting the person by whom the title to the property is held by an equitable duty to convey it to another on the ground that his acquisition or retention of the property would be wrongful and that he would be unjustly enriched if he were permitted to retain the property.

### Resulting Trust

A resulting trust is one, which is implied in favour of the settler or his representative. It comes into existence where the property is incompletely conveyed or where on a conveyance, the beneficial interest in the property is not completely disposed of and the property or the undisposed beneficial interest in it reverts back to the settler. When a trust is bad as a charitable trust, a resulting trust comes into existence in favour of the settler. *[Dwarkadas Bhimji v. CIT (1948) 16/TR 160 Bom.]*

### Executed and Executory Trust

An executed trust is one in which the limitation of the estate and the beneficiaries are prescribed by the settler in the trust deed itself and no further instrument is required.

An executory trust is not complete in itself and its execution is left to the judgement of the trustees. Here, the settler instead of expressing exactly what he means, tells the trustees to do their best to carry out his intentions.

#### State whether the following statement is “True” or “False”

A trust cannot be declared orally and must always be in writing

- True
- False

**Correct Answer:** False

## CREATION OF TRUSTS

### (i) Creation of Trusts for lawful purposes only

The Act allows creation of a trust for any lawful purposes. What is lawful can be gathered from the provisions of Section 4 of the Act which provides that purpose of a trust is lawful unless it is

- (a) forbidden by law, or
- (b) is of such a nature which will defeat the provisions of any law, or
- (c) is fraudulent, or
- (d) involves or implies injury to the person or property of another, or
- (e) the Court regards it as immoral or opposed to public policy.

Thus a trust which does not fall in any of the above prohibitions, is deemed to be for lawful purpose. A trust for an unlawful purpose is void. Where a trust is created for two purposes one lawful and another unlawful, and the purposes are inseparable from one another, the whole trust is void. On the other hand if one of the objects of a trust is lawful and the expenses on it are fixed, and that object is not dependent upon and is separate from the other objects, the trust to that extent will be valid.

The expression 'law' includes the law of a foreign country in which immovable property of a trust is situated.

### (ii) Trust of immovable property

Section 5 of the Act lays down the formalities which are to be observed for creation of a trust. It provides that a trust of immovable property can be created by an instrument in writing and registered, signed by the author of the trust or by Will.

Trust of movable property requires no writing or registration. The mere transfer of possession coupled with the intention of the parties that such delivery of possession should vest the property in the trustee is sufficient to create a trust.

### (iii) Creation of a trust

Section 6 lays down provisions for creating a trust. It provides that subject to the provisions of Section 5 a trust is created when the author of the trust indicates with reasonable certainty by any words or acts: (a) an intention on his part to create thereby a trust; (b) the purpose of the trust; (c) the beneficiary, and (d) the trust property; transfer the trust property to the trustee except where a trust is declared by Will or the author of the trust is himself to be the trustee. If a trust is to be valid and enforceable, it is material to ascertain the author of the trust. Next the intention to create a trust, the purpose of the trust, the trust-property and the beneficiaries must be indicated and in such a way that the trust could be administered by the Court if the occasion arose.

## Certainties of a Trust

For creating a trust the author of the trust should indicate with reasonable certainty the following:

- (1) *Certainty in words:* The words used to create a trust must be clear and certain so as to explain a clear intention to create a trust. Recommendatory words like "I hope" "I wish" are not sufficient.
- (2) *Certainty in the object of the trust :* The beneficiary, for whose benefit the trust is created, must be shown clearly.

- (3) *Certainty in the subject-matter of the trust* : The subject matter of the trust must be clear, i.e., the property, in respect of which a trust is created, must be shown clearly. Purpose of the trust should be certain.

If the trust instrument is lacking in first and third certainties, no trust is created but if the second certainty is absent, resulting trust will be created in favour of the author of the trust.

#### **Illustrations:**

- (a) A bequeaths certain property to B, "having the fullest confidence that he will dispose of it for the benefit of C". This creates a trust so far as regards A and C. B is not bound as a trustee.
- (b) A bequeaths certain property to B, "hoping he will continue it in the family". This does not create a trust as the beneficiary is not indicated with reasonable certainty.
- (c) A bequeaths certain property to B, requesting him to distribute it amongst such members of C's family as B should think most deserving. This does not create a trust, for the beneficiaries are not indicated with reasonable certainty.
- (d) A bequeaths certain property to B desiring him to divide the bulk of it among C's children. This does not create a trust, for the trust property is not indicated with sufficient certainty.
- (e) A bequeaths a shop and stock-in-trade to B on condition that he pays A's debts and a legacy to C. This is condition, not a trust for A's creditors and C.

#### **Who can create a Trust**

A trust may be created (i) by every person competent to contract, and (ii) with the permission of a Principal Civil Court of original jurisdiction, by or on behalf of a minor (Section 7). Thus, generally any person competent to contract and competent to deal with the property can create a trust.

#### **Who may be a Trustee**

Every person capable of holding property may be a trustee. But if the trust involves the exercise of discretion, he cannot execute it unless he is competent to contract (Section 10).

No one is bound to accept a trust. Acceptance of the trust by a trustee may be express or implied.

#### **Illustrations:**

- (a) A bequeaths certain property to B and C, his executors as trustees for D. B and C prove A's will. This is in itself an acceptance of the trust, and B and C hold the property in trust for D.
- (b) A transfers certain property to B in trust to sell it, and to pay out of the proceeds, A's debts. B accepts the trust and sell the property. So far as regards B, a trust proceed is created for A's creditors.
- (c) A bequeaths, a lakh of rupees to B upon certain trusts, and appoints him his executor. B serves the lakh of rupees from the general assets, and appropriates it to the specific purpose.

This is an acceptance of the trust.

#### **Duties of Trustee**

Sections 11 to 22 of the Act deal with the duties of trustee. They are as under:

- (1) The Trustee should execute the trust and obey the directions given in the instrument of the trust. He

can make any alteration in those directions only with the consent of beneficiaries who are competent to contract. If a beneficiary is incompetent to enter into a contract, the Principal Civil Court of original jurisdiction may give consent on behalf of the minor.

**Illustrations:**

- (a) A, a trustee, is simply authorised to sell certain land by public auction. He cannot sell the land by private contract.
  - (b) A, a trustee of certain land for X, Y and Z, is authorized to sell the land to B for a specified sum. X, Y and Z, competent to contract, consent that A may sell the land to C for a lesser sum. A may sell the land accordingly.
  - (c) A, a trustee, for B and her children, is directed by the author of the trust to lend, on B's request, trust property to B's husband, C on the security of his bond. C becomes insolvent and B requests A to make the loan. A may refuse to make it.
- (2) It is a duty of a trustee to acquaint himself with the nature of the trust property.
- (3) The trustee must protect and preserve the trust property.

**Illustrations:**

The trust property is immovable property which has been given to the author of the trust by an unregistered instrument. The trustee's duty is to cause the instrument to be registered.

- (4) The trustee must not set up a title to the trust property, which is adverse to the interest of the beneficiary. Nor should he allow any person to do so.
- (5) He must deal with the trust property in such a manner as a man of ordinary prudence would deal with such property as if it were his own.

**Illustrations:**

- (a) A, a trustee for B, in execution of trust sells trust property but for want of due diligence on his part, fails to receive part of the purchase money. A is bound to make good the loss.
- (b) A, trustee for B, allows the trust to be executed solely by his co-trustee C. C misapplies the trust property. A is personally answerable for the loss resulting to B.
- (6) If a trust is created in favour of several persons in succession and the trust property is of washing nature or consists of a future or reversionary interest, the trustee is bound to convert it into property of permanent nature. However, this is subject to any contrary intention which could be inferred from the trust instrument.

**Illustrations:**

A bequeaths to B all his property on trust for C during his life, and on his death for D, on D's death for E. A's property consists of three leasehold houses and there is nothing in A's will to show that he intended the houses to be enjoyed in *specie*. B should sell the houses and invest the proceed in trust securities as per Section 20.

- (7) The trustee must act impartially where there are more than one beneficiary.
- (8) Where the trust is created for the benefit of several persons in succession and one of them is in possession of the trust property, if that person commits any act destructive or injurious to the trust property, the trustee must take the steps to prevent it.

- (9) The trustee must keep an accurate account of the trust property. At the request of the beneficiary he must furnish him the account and the state of trust property.
- (10) The trustee must invest the trust property and funds in the securities mentioned in Section 20 of the Act. This is subject to any contrary directions in the trust instrument.
- (11) The trustee must sell the trust property within the specified or extended time without prejudice to the beneficiary or as authorized by the Court.

### Liabilities of Trustees

1. **Liability for a breach of Trust:** If a trustee commits a breach of the trust, he is liable to make good the loss which the trust property of the beneficiary has suffered. However, in two cases he is not liable for such a loss. (i) Where the breach of the trust has resulted due to any fraud committed by the beneficiary; and (ii) Where the beneficiary, being competent to contract, has given his consent for that breach without any coercion or undue influence or subsequently acquiesced therein, with full knowledge of the facts (Section 23).

### Illustrations:

- (a) A trustee improperly leaves trust property outstanding, and if it is consequently lost he is liable to make good the property lost, but he is not liable to pay interest thereon.
  - (b) A trustee is guilty of unreasonable delay in investing trust money in accordance with Section 20, or in paying it to the beneficiary. The trustee is liable to pay interest thereon for the period of the delay.
  - (c) The instrument of trust directs the trustee to invest trust money either in any of such securities or on mortgage of immovable property. The trustee does neither. He is liable for the principal money and interest.
  - (d) The trust property consists of land. The trustee sells the land to a purchaser for a consideration without notice of the trust. The trustee is liable at the option of the beneficiary, to purchase other land of equal value to be settled upon the like trust, or to be charged with the proceeds of the sale with interest.
2. **No right of set-off:** A trustee who is liable for a loss because of a breach of trust committed by him in respect of one portion of the trust property is not allowed to set-off against his liability, a gain which he has accrued to another portion of the trust property through another and distinct breach of the trust property (Section 24).
  3. A trustee is not liable for the acts and defaults of his predecessor.
  4. Generally a trustee is not liable for a breach of the trust committed by his co-trustee. However, such a trustee will be liable in the following cases:
    - (i) Where he delivers his trust property to his co-trustee without seeing to its proper application;
    - (ii) Where he allows his co-trustee to receive the trust property and fails to make due inquiries about his co-trustee's dealing therewith; and
    - (iii) Where after he comes to know of the breach of the trust committed by his co-trustee, he either actively conceals it or does not take proper steps to protect the interest of the beneficiary.

However, a co-trustee who joins in signing a receipt for the trust property for sake of conformity without actually receiving it shall not be liable merely by reason of his signature only.

A trustee is liable for money and property actually received by him.

5. *Nature of liability of a co-trustee* : When co-trustees jointly commit a breach of trust, and when one of them, by his negligence, enables another trustee to commit a breach of trust, each trustee is liable to the beneficiary for the whole loss sustained by the beneficiary.
6. Under Section 23 of the Act, in certain circumstances, a trustee is liable to pay simple or compound interest to the beneficiary.

### **Rights, Powers and Disabilities of Trustees**

The rights, powers and disabilities of a trustee are discussed in Chapter IV of the Act. The important *rights* are as under:

1. The right to have the possession of the instrument of trust and the title-deed relating to the trust property.
2. The right to reimburse himself of all costs, expenses and liabilities incurred in administration of the trust.
3. In case of a breach of the trust, the person who derives any benefit out of such a breach, must indemnify, the trustee to the extent of the amount actually received by him.
4. A trustee has a right to take opinion, advice or direction from the Court on questions relating to the management and administration of the trust.
5. When a trustee, properly completes his duties, he is entitled to get a discharge to the effect in writing.
6. A trustee has a general right to do all necessary acts (i) for preservation and protection of the trust property, and (ii) to protect the interest of a beneficiary who is not competent to contract but he cannot give on lease any trust property for more than twenty-one years without the permission of a Court.

### **Powers of Trustee**

1. He can sell the trust property where instrument of the trust so empowers him.
2. A trustee has a power to vary investments.
3. A trustee has a power to apply the trust property for the maintenance of property as provided in the instrument of trust.
4. A trustee can compromise claims unless a contrary intention appears from the instrument of the trust.
5. A trustee can give receipt for the money received on account of the trust.
6. In case of death of one of the trustees, the other trustees have a right to act, unless contrary intention appears from the instrument of the trust.

### **Disabilities of Trustees (Chapter V)**

1. A trustee who once accepted the trust, cannot renounce it except:
  - (i) with the permission of the Court,
  - (ii) with the consent of the beneficiaries who are competent to contract,
  - (iii) by virtue of a special power in the instrument of the trust.

2. A trustee cannot delegate his office or any of his duties either to a co-trustee or to a stranger, except in the following cases:
- (1) When the instrument of the trust so provides,
  - (2) When such a delegation is in the regular course of business,
  - (3) When such a delegation is necessary, and
  - (4) The beneficiary, being competent to contract, consents to such a delegation.

#### **Illustrations:**

- (a) A bequeaths certain property to B and C on certain trust to be executed by them or the survivor of them or the assigns of such survivor, B dies. C may bequeath the trust property to D and E upon the trusts of A's will.
  - (b) A is a trustee of certain property with power to sell the same. A may employ an auctioneer to effect the sale.
  - (c) A bequeaths to B fifty houses let at monthly rents in trust to collect the rents and pay them to C. B may employ a proper person to collect these rents.
3. Where there are more trustees than one, all must join in the execution of the trust unless the trust instrument or any law for the time being in force provides otherwise.
  4. The trustees cannot exercise their discretionary powers arbitrarily.
  5. In the absence of express direction to the contrary contained in the instrument of trust or of a contract entered into with the beneficiary or of the sanction of the Court, the trustee has no right to remuneration.
  6. A trustee may not use or deal with the trust property for his own use.
  7. No trustee whose duty is to sell the trust property may directly or indirectly buy the trust property.
  8. No trustee and no person who has recently ceased to be a trustee may, without the permission of the Court, buy, or become mortgagee or lessee of the trust property.
  9. The trustee and the co-trustee may not lend the trust amount to themselves.

#### **Vacating the office of trusteeship**

The office of a trustee is vacated on his death or by his discharge. He may be discharged from his office by the extinction of the trust or by the completion of his duties or by new appointee etc.

#### **Meaning of a Beneficiary**

The person or persons for whose benefit, a trust has been created, is called the beneficiary or beneficiaries. While the trustees hold the legal title in trust property, the beneficiary holds the beneficial interest in that property.

#### **Who may be a beneficiary**

A beneficiary may be any person, so specified by the author of the trust, a beneficiary may be a near or distant relative of the author or a person not related to the author at all or general public or a class thereof. A minor, woman and even an unborn person can be a beneficiary. In case of a charitable or religious trust, there need not be a specific beneficiary; the beneficiary thereunder is the object or the purpose of the trust.

If the beneficiaries under a trust are not specified and they are not capable of being ascertained, no trust can come into existence [*Allahabad Bank v. CIT AIR 1953 476*].

A beneficiary may renounce his interest under the trust by (i) a disclaimer addressed to the trustee or (ii) by setting up a claim inconsistent with the trust. On the disclaimer by a beneficiary and the trust deed does not provide for such disclaimer, the trust would revert to the author or settler as a resulting trust.

**Choose the correct answer**

Which of the following persons can be a beneficiary?

- (a) A minor
- (b) A woman
- (c) An unborn person
- (d) All of the above

**Correct Answer:** (d)

**Doctrine of Cypres**

Where the object of the charitable trust, specified by the settler, is or subsequently becomes impossible or impracticable or unlawful, the trust will not necessarily fail, but the Court has power to apply the trust to some other charitable object as nearly as possible resembling the intention of the author. This power of the Court is known as "doctrine of cypres". When a particular mode of charity indicated by the author is not capable of being carried out, yet a general intention of charity, is indicated by the author of the trust, the Court would execute it 'cypres' i.e. in a way as nearly as possible to that which testator specified.

**Rights and Liabilities of Beneficiaries (Chapter VI)**

Important rights of the beneficiary of the trust are:

1. Right to rents and profits of the trust-property;
2. Right to the specific execution of the trust;
3. Right to inspect and take copies of the instrument of trust;
4. Right to transfer the beneficial interest, if he is competent to contract;
5. Right to sue for execution of trust;
6. Right to proper trustees; and proper number of trustees;
7. A beneficiary has a right to follow the trust property in the hands of a third person. Even where a trustee disposes of the trust property and acquires some other property with the help of the disposal money, the beneficiary is entitled to have the latter property, the same rights or as nearly as possible the same rights, he had over the trust property.

**Illustrations:**

- (a) A, a trustee for B wrongfully invests ` 10,000 in the purchase of certain land, B is entitled to the land.
- (b) A, a trustee, wrongfully purchases land in his own name, partly with his own money, partly with money subject to a trust for B. B is entitled to a charge on the land for the amount of the trust money so misemployed.
- 8. Right to compel to any act of duty.

## Liabilities:

If a beneficiary commits a breach of trust or obtains any advantage, the other beneficiaries may attach the interest of such a beneficiary until the loss caused by the breach has been compensated.

## Extinction of a Trust (Section 77)

A trust is extinguished:

- When its purpose is completely fulfilled; or
- When its purpose becomes unlawful; or
- When the fulfillment of its purpose becomes impossible by destruction of the trust property or otherwise; or
- When the trust being revocable, is revoked.

## Revocation of a Trust (Section 78)

If a trust is created by a Will, it may be revoked by the revocation of the Will. A trust which has been created otherwise, by an instrument other than a Will or orally, can be revoked only:

- with the consent of all the beneficiaries competent to contract;
- by the exercise of power of revocation expressly reserved by the author of the trust (in cases of trusts declared orally or by non-testamentary instruments); or
- where the trust is created for the payment of debts of the author of the trust, and has not been communicated to the creditors, at the pleasure of the author of the trust.

A conveys property to B in trust to sell the same, and pays out of the proceeds the claims of A's creditors. A reserves no power of revocation. If no communication has been made to the creditor. A may revoke the trust. But if the creditors are parties to the agreement, the trust cannot be revoked without their consent.

A trust is generally irrevocable unless a power of revocation is expressly reserved.

## LESSON ROUND UP

- A 'trust' is an obligation annexed to the ownership of property and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another or of another and the owner.
- Indian Trust Act has no application to public or private, religious or charitable endowment.
- Trust in its origin was a form of contract distinctively enforced in equity. A contract creates a trust where it has brought into existence an obligation annexed to the ownership of property for the benefit of a person other than the owner.
- A trust may be created (i) by every person competent to contract, and (ii) with the permission of a Principal Civil Court of original jurisdiction, by or on behalf of a minor.
- Every person capable of holding property may be a trustee. But if the trust involves the exercise of discretion, he cannot execute it unless he is competent to contract.
- The person or persons for whose benefit, a trust has been created, is called the beneficiary or beneficiaries. While the trustees hold the legal title in trust property, the beneficiary holds the beneficial interest in that property.
- A trust is extinguished when its purpose is completely fulfilled or when its purpose becomes unlawful or when the fulfillment of its purpose becomes impossible by destruction of the trust property or otherwise or When the trust being revocable, is revoked.

## SELF TEST QUESTION

1. Define a 'trust'. Distinguish a trust from a contract.
  2. How a trust is created and by whom it is created?
  3. Briefly discuss the provisions relating to rights and duties of trustees.
  4. Who is a beneficiary? What are his rights and liabilities?
  5. Write short notes on
    - (i) Extinction of a trust
    - (ii) Revocation of a trust
    - (iii) Doctrine of *Cy Pres*.

# Lesson 13

## INDUSTRIES DEVELOPMENT AND REGULATION

### Section I

#### LESSON OUTLINE

- Industrial Undertaking
- Factory
- New Article
- Existing Industrial Undertaking
- Industrial Policy Resolution, 1948
- Industrial Policy Resolution 1956
- New Industrial Policy, 1991
- Central Advisory Council
- Development Council
- Existing Industrial Undertaking
- Industrial licence
- Substantial expansion
- Direction for investigation
- Investigation into Scheduled Industries/Industrial Undertakings
- Take-Over of Industrial Undertakings
- Power of Central Government
- Liquidation or Reconstruction of Companies
- Cognizance of Offences
- Offences and Penal

#### **LEARNING OBJECTIVES**

Industrialization is a major objective of developing countries as a means to the attainment of higher levels of economic well-being of the people. Growth of the industrial sector at a higher rate and on a sustained basis is a major determinant of a country's overall economic development. In this regard, the Government of India has issued industrial policies, from time to time, to facilitate and foster the growth of Indian industry and maintain its productivity and competitiveness in the world market.

Immediately after independence, Government adopted in 1948 an Industrial Policy Resolution, a historic document and a trend setter, which emphasised on importance to the economy of securing a continuous increase in the production and its equitable distribution and pointed out that State must play a progressively active role in the development of industries. The Industrial Policy Resolution 1948 was provided legal support by enacting Industries (Development and Regulation) Act, 1951.

The main objectives of the Act is to empower the Government to take necessary steps for the development of industries; to regulate the pattern and direction of industrial development; to control the activities, performance of industrial undertakings in the public interest. Therefore, it is essential for the students to be familiar with the law relating to enacting Industries (Development and Regulation) Act, 1951.

The preamble to the Act states that Industries (Development and Regulation) Act, 1951 is an Act 'to provide for the development and regulation of certain industries'. These industries are specified in the First Schedule to the Act.

## INTRODUCTION

Industrialization is a major objective of developing countries as a means to the attainment of higher levels of economic well-being of the people. Advancement of science and technology provides the wherewithal to achieve faster industrial growth.

After four and half decades of strongly inward oriented policies, India began opening up of its economy to foreign trade and investment with the announcement of New Industrial Policy in July 1991. The New Industrial Policy seeks to prepare Indian industry for meeting the challenges of globalisation. The reforms aim at generating a market orientation for the hitherto highly regulated domestic economy by deregulating the domestic economy to provide Indian industry with greater flexibility to respond to competitive pressures by reducing costs and improving quality.

The New Industrial Policy has injected a substantial measure of competitive environment and market thrust to industry. Many areas earlier reserved for the public sector are now open to private sector participation. The restrictions on the expansion of large industrial houses have been removed. Licensing requirements for industries have been abolished except for a few strategic and defence industries.

The policy reforms towards Foreign Direct Investment (FDI) began with a radically new approach to FDI in the very first year of the implementation of New Industrial Policy. The new regime permits FDI in virtually every sector of the economy. Foreign equity proposals need not be accompanied by technology transfer as required earlier. Royalty payments have been considerably liberalised, and restrictions on the use of foreign brand name/trademarks for internal sale have been removed.

Before going into the details of regulation of Indian industries, let us have a look at the successive industrial policies adopted by the Government.

### Industrial Policy Resolution, 1948

Immediately after independence, the Government gave a careful thought to the economic problems faced by India and recognised that any improvement in the economic conditions of the people is possible only through a substantial increase in the generation of national wealth as a mere distribution of existing wealth would not make any significant difference to the people. Thus, a need for a dynamic national policy directed towards a continuous increase in production and productivity by all possible means, together with measures to secure its equal distribution was felt. The Government in this context adopted in 1948 an Industrial Policy Resolution, a historic document and a trend setter, which emphasised on importance to the economy of securing a continuous increase in the production and its equitable distribution and pointed out that state must play a progressively active role in the development of industries.

The resolution envisioned that besides arms, ammunition, atomic energy and railway transportation, to be the monopoly of the Central Government, the States would be exclusively responsible for the establishment of new undertakings in basic industries except where, in the national interest, the State itself found it necessary to secure the cooperation of private enterprise. The rest of the industrial areas were thrown open to private enterprise, though it was made clear that the State would also progressively participate in these fields.

Recognising the valuable role of private enterprise in the economy, the resolution emphasised that the States could contribute more quickly to the increase of national wealth by expanding its present activities where it is already operating and by concentrating on new units of production in other fields, rather than acquiring and running existing units. The resolution also recognised the importance of participation of foreign

capital and enterprise, particularly in relation to industrial technology and knowledge, for the rapid industrialisation of India. The Industrial Policy Resolution 1948 was provided legal support by enacting Industries (Development and Regulation) Act, 1951 and vesting in the Government necessary powers to regulate and control the existing and future undertakings.

### **Industrial Policy Resolution, 1956**

The Industrial Policy Resolution of 1956 laid down the basic approach towards industrial development. The policy thrust rightly recognised the Directive Principles of State Policy enshrined in the Constitution and the adoption by the Parliament in December 1954 of the socialist pattern of society as the objective of social and economic policy.

In order to realise the socialistic pattern of society, the Government recognised the need to accelerate the rate of economic growth and to speed up industrialisation and, in particular, to develop heavy industries and machine making industries, to expand the public sector. The Government also felt the need to prevent private monopolies and the concentration of economic power in different fields in the hands of small number of individuals.

The Government classified industries into three categories. The first category included those industries the future development of which was the exclusive responsibility of States. The second category included progressively State owned industries and areas in which the States had to take initiatives to establish new undertakings, though the private participation was also expected to supplement the Government efforts. The third category included all the remaining industries with the responsibility of private sector for their development.

The Industrial Policy Resolution of 1956 was followed by the Industrial Policy Statement of 1973 which, inter alia, identified high priority industries for investment by large Industrial houses and foreign companies. Emphasis on de-centralisation and on the role of small scale, tiny and cottage industries was the hallmark of the Industrial Policy Statement of 1977. The Industrial Policy Statement of 1980 focussed attention on the need for promoting competition in the domestic market, technological upgradation and modernisation. The policy laid down the foundation for an increasingly competitive export base and for encouraging foreign investment in high technology areas. These policies created a climate for rapid industrial growth in our country. A number of policy and procedural changes were also introduced in the years 1985 and 1986 aimed at increasing productivity, reducing costs and improving quality.

### **New Industrial Policy, 1991**

The New Industrial Policy was tabled in the Parliament on 24th July, 1991, at the time when the Government of India faced severest foreign exchange resource crunch. This document admitted candidly the policy distortions of the past and expressed the Government's earnestness to achieve a break through in its policy formulations.

The statement on New Industrial Policy states that the major objectives of the new Industrial Policy package will be to build on the gains already made, correct the distortions or weaknesses that may have crept in, maintain a sustained growth in productivity and gainful employment and attain international competition..... Pursuant to this, the Government initiated a series of measures in the areas of Industrial licensing, foreign investment, foreign technology agreements, public sector policy and the MRTP Act.

The Industrial Policy Resolution of 1956 and the statement on new Industrial Policy of 1991 provide the basic framework for overall industrial policy of the Government. Over the years, adjustments have been made in the policy to accelerate the pace of industrial growth by providing greater freedom in investment decisions

keeping in view the objectives of efficiency and competitiveness, technological upgradation, maximisation of capacity utilisation and increased growth.

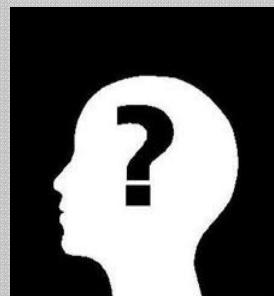
The thrust of the New Industrial Policy of 1991 has, therefore, been to inject new dosage of competition in order to induce greater industrial efficiency and international competitiveness. The domestic competition has been induced by delicensing of industries and liberalising the policy related to foreign direct investment.

Since July 1991, the Indian industry has undergone a sea change in terms of the basic parameters governing its structure and functioning. The major reforms include large scale reduction in the scope of industrial licensing, simplification of procedural rules and regulations, reduction of areas reserved exclusively for the public sector, disinvestment of equity in selected public sector undertakings, enhancing the limits of foreign equity participation in domestic industrial undertakings, liberalisation of trade and exchange rate policies, rationalisation and reduction of customs and excise duties and personal and corporate tax.

With a view to ensure efficient allocation of resources, banking and capital markets also came in for major economic reforms. The banking sector reforms included substantial interest rate deregulation, liberal licensing of private sector banks, and expansion of the branch network of foreign banks. The capital market reforms aimed at de-linking capital market from direct government controls, by a system of better disclosure, greater transparency and wider investor protection. Separate policy measures were announced in the form of specific packages aimed at upliftment of the small scale, tiny and cottage industries as well as 100% Export Oriented Units, and units located in the Export Processing Zones and Technology Parks and Special Economic Zones.

***What are the objectives of Industrial Policy of the Government?***

- To maintain a sustained growth in productivity;
- To enhance gainful employment;
- To achieve optimal utilisation of human resources;
- To attain international competitiveness; and
- To transform India into a major partner and player in the global arena.



***The Policy focus is on –***



- Deregulating Indian industry;
- Allowing the industry freedom and flexibility in responding to market forces; and
- Providing a policy regime that facilitates and fosters growth of Indian industry

***The Industries (Development & Regulation) Act, 1951***

The Industries (Development and Regulation) Act, 1951 is an important piece of legislation affecting the industrial sector of the country.

The object of Industries (Development and Regulation) Act [I (D&R) Act] is to provide to the Central Government means of implementing the Industrial Policy. It seeks to regulate the deployment of material resources of the community according to the norms laid down in the Policy and is thus an instrument for its implementation. The Act has helped the Government in directing the manner in which industrial development

should take place in the country and also in optimising the development of scarce resources of the community amongst competing claims.



*The preamble to the Act states that the I (D&R) Act is an Act 'to provide for the development and regulation of certain industries'. These industries are specified in the First Schedule to the Act. The scope of the Act is therefore, limited to the industries mentioned in the First Schedule known as 'scheduled industries'.*

The term 'industry' is not defined under the Act though the term 'industrial undertaking' is. The scope of the regulatory provisions in the Act is more specific and limited in respect of 'industrial undertakings' which fall within the industries mentioned in the First Schedule.

The system of licensing provided under the Act regulates the planning of future development and undertakings on sound lines as may be deemed expedient in the opinion of the Central Government. The Act confers on the Central Government power to make rules for registration of existing undertakings, regulation of the production and development of industries specified in the Schedule attached to the Act.

### **Implementation of the Act**

The Act is implemented through Department of Industrial Policy and Promotion, Ministry of Commerce & Industry on whom the Central Government has vested the power to develop and regulate Scheduled Industries.

I(D&R) Act is simple in its text and deals only with principles, leaving the details to be worked out by the authorities entrusted with the task of translating them into concrete action plans. This has resulted in the issue of various notifications, circulars, press notes, clarifications from time to time by the hitherto Department of Industrial Development now named as Department of Industrial Policy and Promotion with a view to administering the Act.

The Central Government has framed the Registration and licensing of Industrial Undertakings Rules, 1952, prescribing general procedure to be followed for the purposes of registration and licensing of an industrial undertaking.

### **Scheme of the Act**

The Act can be divided into two parts: (i) those dealing with developmental aspects and (ii) those dealing with regulatory aspects of scheduled industries. The development of the Scheduled Industries is sought to be secured primarily through the agencies of Central Advisory Council and Development Councils as well as by offering certain special facilities that the Government may consider necessary.

Regulation of these industries is sought to be done by means of a system of registration of existing undertakings, licensing of new undertakings for producing new articles and for substantial expansion or change of location of existing undertakings.

Control over the industries is sought to be exercised by causing investigation into the working of these industries and in appropriate cases taking over of direct management and control.

The Act, however, empowers the Central Government to grant exemptions to any undertaking or a scheduled industry or class of undertakings or scheduled industries from all or any of the provisions of the Act, Rules or Orders made thereunder. Exemptions under Section 29B are granted having regard to the number of workers employed in, or the amount invested in, any industrial undertaking or the desirability of encouraging small undertakings generally or the stage of development of any scheduled industry.

## DEFINITIONS

Section 3 of the Act defines some of the terms used in the Act and clarifies that the words and expressions used in the Act and not defined thereunder but defined in the Companies Act, 1956 shall have the meanings respectively assigned in that Act. Before going into the study of the provisions of the Act it would be necessary to look into the meaning and scope of some of the important terms used in the Act.

### Existing Industrial Undertaking

Section 3(bb) of the Act defines the term existing industrial undertaking as to mean (a) in the case of an industrial undertaking pertaining to any of the industries specified in the First Schedule as originally enacted, an industrial undertaking which was in existence on the commencement of this Act or for the establishment of which, effective steps had been taken before such commencement, and (b) in the case of an industrial undertaking pertaining to any of the industries added to the First Schedule by an amendment thereof, an industrial undertaking which is in existence on the coming into force of such amendment or for the establishment of which, effective steps had been taken before the coming into force of such amendment.

In this context, Rule 2 of the Registration and Licensing of Industrial Undertakings Rules, 1952 defines 'effective steps' to mean one or more of the following:

- (a) 60% or more of the capital issued for an industrial undertaking which is a public company within the meaning of the Companies Act, 1956, has been paid up;
- (b) a substantial part of the factory building has been constructed;
- (c) a firm order has been placed for a substantial part of the plant and machinery required for the undertaking.

To be an 'existing industrial undertaking' the undertaking must pertain to an industry specified in the First Schedule i.e. it must have been set up to manufacture articles which can be said to fall in an item in the First Schedule.

### Factory

The term factory has been defined under Section 3(c) of the Act and includes any premises including the precincts thereof in any part of which a manufacturing process is being carried on or is ordinarily so carried on (i) with the aid of power provided that 50 or more workers are working or were working thereon on any day of the preceding twelve months, or (ii) without the aid of power provided that 100 or more workers are working or were working thereon on any day of the preceding twelve months and provided further that in no part of such premises any manufacturing process is being carried on with the aid of power.

The term 'manufacturing process' has not been defined under the Act. Although what constitutes 'manufacturing process' will depend on the facts and circumstances of each case, it can be said as a first principle that, in order to constitute 'manufacture', there must be a transformation. Merely labour bestowed on an article even if the labour is applied through machinery will not make it a manufacture unless it has progressed so far that transformation ensues, and the article becomes commercially known as another and different article from that with which it begins its existence. [A.M. Chinniah, Manager, Sangu Soap Works, AIR (1957) Mad. 755].

In *Delhi Cloth and General Mills Co. Ltd. v. Joint Secretary, Govt. of India* (1978) Tax L.R. 2094, it had been held that it was not necessary that the manufacturing process should be carried on in the whole of the premises and that even if part of the premises was used for manufacturing process the other could as well be included in factory premises.

## Industrial Undertaking

Section 3(d) of the Act defines industrial undertaking to include any undertaking pertaining to a scheduled industry carried on in one or more factories by any person or authority including Government.

Therefore, according to the definition, the undertaking must not only pertain to a scheduled industry but also should be carried on in one or more 'factories' within the meaning of Section 3(c) of the Act. That means, where the number of workers employed is less than 50 where power is used or, less than 100 where no power is used, it would not be considered to be factory under the Act and consequently, it would not be an 'industrial undertaking' for the purposes of this Act. Though the word 'undertaking' is not separately defined in the Act, the basic feature expected to be present to constitute an undertaking is the existence of a factory as defined in the Act where some manufacturing process is carried on.

## New Article

Section 3(dd) says that new article in relation to an industrial undertaking which is registered or in respect of which a licence or permission has been issued under this Act means: (a) any article which falls under an item in the First Schedule other than the item under which articles ordinarily manufactured or produced in the industrial undertaking at the date of registration or issue of the licence or permission as the case may be, fall; (b) any article which bears a mark as defined in the Trade Marks Act or which is subject of a patent, if at the date of registration or issue of the licence or permission, as the case may be, the industrial undertaking was not manufacturing or producing such article bearing that mark or which is the subject of that patent.

Broadly speaking therefore, an article, the manufacture of which would not be covered by the existing industrial licence would be a 'new' article. Where the article to be manufactured is covered under existing licence of the manufacturer by virtue of any broadbanding facility announced by the Government, it would not be termed as a 'new' article. But in case the new article to be manufactured bears a new trade mark or a patent, a fresh licence would be required even if the article falls under the same item in the First Schedule for which the undertaking already possesses a licence.

In order to show that the proposed manufacture of an article is a proposal for manufacturing a new article, it should be proved that the proposed article cannot be brought within the item under which the article being manufactured presently falls. Where, it can be shown that the proposed article falls under a different item of the First Schedule, it would constitute a new article. It may be noted that soon after the introduction of the definition of the term 'New article' in the Act, the Licensing Committee had pointed out that a broad and reasonable view of the term should be taken and that where no new trade mark or no new patent was involved and the product was covered within the ambit of the same item in the First Schedule under which the concerned undertaking held a registration certificate or industrial licence, the article of proposed manufacture would not be considered as a new article and there should be no objection to the owner of the industrial undertaking manufacturing it. The term 'New article' assumes significance and importance in the context of Section 11A which casts an obligation upon the owner of an industrial undertaking to obtain a licence for producing or manufacturing new articles.

## Owner

The term owner under Section 3(f) has been defined to mean the person who, or the authority which, has the ultimate control over the affairs of the undertaking and where the said affairs are entrusted to a manager, managing director or managing agent, such manager, managing director or managing agent shall be deemed to be the owner of the undertaking.

It may be noted that the term 'person' employed in the definition would include both natural and artificial

persons. Bodies corporate owning industrial undertakings would also be covered within the above definition. While this definition makes it clear that any person or authority having ultimate control over the affairs of the undertaking is the owner, it also introduces a deeming provision whereby certain categories of persons in whom the affairs of the industrial undertaking may be entrusted are declared to be owners.

Thus, a company owning an industrial undertaking would be the person having 'ultimate' control over the affairs of the undertaking, but where it has appointed a manager who has the management control of the whole, or substantially the whole of the affairs of the company, he will also be deemed to be the 'owner'.

The term 'owner' has particular relevance and significance in the context of the provisions of Sections 5, 6, 10, 10A, 11A, 13 as well as Section 18F. It should also be noted that reference to managing agent in the definition is not of any significance now on account of the fact that the system of managing agency has since been abolished.

### **Scheduled Industry**

Section 3(i) defines the term Scheduled industry to include any of the industries specified in the First Schedule of the Act.

### **Current Assets**

The term current assets has been defined under Section 3(ab) of the Act to include bank balance and cash and such other assets or reserves as are expected to be realised in cash, or sold or consumed within a period of not more than 12 months in the ordinary course of business, such as, stock-in-trade, amounts due from sundry debtors for sale of goods and services rendered, advance tax payments and bills receivable, but does not include sums credited to a provident fund, a pension fund, a gratuity fund or any other fund for the welfare of the employees, maintained by a company owning an industrial undertaking.

### **Current Liabilities**

Section 3(ac) defines the term current liabilities as to mean liabilities which must be met on demand or within a period of twelve months from the date they are incurred; and includes any current liability which is suspended under Section 18FB.

### **Central Advisory Council**

Section 5 of the Act empowers the Central Government to establish by notified order, a council to be called the Central Advisory Council, for advising the Government on matters concerning the development and regulation of scheduled industries. Section 5(2), deals with composition of Advisory Council and provides that it shall consist of a chairman and such other members not exceeding thirty in number, to be appointed by the Central Government from among persons who are, in its opinion, capable of representing the interest of owners of industrial undertakings in Scheduled Industries; persons employed in industrial undertakings in Scheduled Industries; consumers of goods manufactured or produced by Scheduled Industries; and such other class of persons including primary producers, as in the opinion of the Central Government ought to be represented on the Advisory Council.

### **Development Council**

Section 6 of the Act also empowers the Central Government to establish by notified order, a body of persons to be called a Development Council consisting of such members who, in the opinion of the Central Government, are persons capable of representing the interests of owners of industrial undertakings in the scheduled industry or group of scheduled industries; persons having special knowledge of matters relating to

the technical or other aspects of the scheduled industry or group of scheduled industries; persons capable of representing the interests of persons employed in industrial undertakings in the scheduled industry or group of scheduled industries; and persons not belonging to any of the aforesaid categories, who are capable of representing the interests of consumers of goods manufactured or produced by the scheduled industry or group of scheduled industries.

The Central Government may assign to a Development Council, any of the functions specified in the Second Schedule to the Act in order to increase the efficiency or productivity in the scheduled Industry or group of scheduled Industries for which the Development Council is established, improve or develop the service that such industry or group of industries renders, or enable such industry or group of industries to render such service more economically. The functions which may be assigned to Development Council include:

- (i) Recommending targets for production, coordinating production programmes and reviewing progress from time to time.
- (ii) Suggesting norms of efficiency with a view to eliminating waste, obtaining maximum production, improving quality and reducing costs.
- (iii) Recommending measures for securing the fuller utilisation of installed capacity and for improving the working of the industry, particularly of the less efficient units.
- (iv) Promoting arrangements for better marketing and helping in the devising of a system of distribution and sale of the produce of the industry which would be satisfactory to the consumer.
- (v) Promoting standardisation of products.
- (vi) Assisting in the distribution of controlled materials and promoting arrangements for obtaining materials for the industry.
- (vii) Promoting or undertaking inquiry as to materials and equipment and as to methods of production, management and labour utilisation, including the discovery and development of new materials, equipment and methods and of improvement in those already in use, the assessment of the advantages of different alternatives and the conduct of experimental establishments and of tests on a commercial scale.
- (viii) Promoting the training of persons engaged or proposing engagement in the industry and their education in technical or artistic subjects relevant thereto.
- (ix) Promoting the retraining in alternative occupations of personnel engaged in or retrenched from the industry.
- (x) Promoting or undertaking scientific industrial research, research into matters affecting industrial psychology and research into matters relating to production and to the consumption or use of goods and services supplied by the industry.
- (xi) Promoting improvements and standardisation of accounting and costing methods and practices.
- (xii) Promoting or undertaking the collection and formulation of statistics.
- (xiii) Investigating possibilities of decentralising stages and processes of production with a view to encouraging the growth of allied small scale and cottage industries.
- (xiv) Promoting the adoption of measures for increasing the productivity of labour, including measures for securing safer and better working conditions and provisions and improvement of amenities and incentives for workers.

- (xv) Advising on any matter relating to the industry (other than remuneration and conditions of employment) as to which the Central Government may request the Development Council to advise and undertaking inquiries for the purpose of enabling the Development Council so to advise.
- (xvi) Undertaking arrangements for making available to the industry information obtained and for advising on matters with which the Development Councils are concerned in the exercise of any of their functions.

Section 7 requires the Development Council to prepare and transmit to the Central Government and the Advisory Council annually a report (including a statement on the audited accounts together with a copy of audit report) on its functions during the financial year last completed. A copy of each such report shall be laid before Parliament by the Central Government.

Section 9 empowers the Central Government to levy and collect cess on all goods manufactured and produced in any specified scheduled industry and hand over the proceeds to the Development Council established for that industry. The Development Council, in turn, is required to utilise the proceeds, to promote scientific and industrial research with reference to the scheduled industry or group of scheduled industries in respect of which the Development Council is established; to promote improvements in design and quality with reference to the products of such industry or group of industries; to provide for the training of technicians and labour in such industry or group of industries; and to meet such expenses as specified for exercise of its functions including its administrative expenses.

### **Regulation of Scheduled Industries**

Regulation of industries specified in the First Schedule to the Act is sought to be achieved by means of registration of existing industrial undertakings; licensing of new industrial undertakings; and licensing for producing or manufacturing new articles. Registration and licensing procedure has been provided in the Act for the obvious purpose of channelising the limited resources of the country in a manner conducive to the overall industrial development of the country. The Act requires industrial licence to be obtained from the Central Government for certain specific purposes.

### **Registration of Existing Industrial Undertakings**

Section 10 requires the owner of every existing industrial undertaking (not being the Central Government) to register the undertaking in the prescribed manner within the prescribed period. The Central Government has also been put under obligation to register its own existing industrial undertakings. On such a registration the owner of the undertaking is issued a certificate of registration containing the productive capacity of the industrial undertaking and other prescribed particulars.

The concept of existing industrial undertaking may be understood with the help of an illustration. Graphite Crucible was added as Item No. 8 under the head 34 Ceramics in the First Schedule to the Act with effect from 30.12.1978. All industries engaged in manufacture of graphite crucibles on 30.12.1978 and all such industries in respect of which effective steps had been taken on 30.12.1978 for establishment thereof would become existing industrial undertakings within the meaning of the Act.

### **Issue of Certificate of Registration**

Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, after such investigation as it may consider necessary, grants the applicant a certificate of registration containing, besides other prescribed particulars, the productive capacity of the undertaking. In specifying the productive capacity in the

certificate of registration, the Central Government takes into consideration the following matters:

- (i) the productive or installed capacity of the undertaking as specified in the application for registration;
- (ii) level of production immediately before the date on which the application for registration was made;
- (iii) the level of the highest annual production during the preceding three years;
- (iv) the extent to which production during the said period was utilised for export;
- (v) such other factors as the Central Government may consider relevant including the extent of under-utilisation of capacity, if any during the relevant period due to any cause.

### **Circumstances When Registration is Not Necessary**

It may be noted that registration of an undertaking will not be necessary if the undertaking (i) is a small scale industrial undertaking or (ii) is otherwise exempt from the licensing/registration provisions of the Act or (iii) where the undertaking concerned is not satisfying the definition of the term 'factory' under the Act.

### **Penalty For Failure to Register**

The owner of an industrial undertaking which is registrable but has not been registered as required under Section 19(1) of the Act, is liable to be punished under Section 24 of the Act with imprisonment up to six months or fine, which may extend to 5,000 Rupees or with both.

### **Power to Revoke Registration**

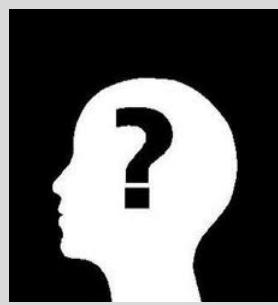
The Central Government has been empowered to revoke the registration if it is satisfied that (i) it was obtained by misrepresentation as to essential facts; or (ii) the undertaking has ceased to be registrable by reason of any exemption granted under this Act; or (iii) for any other reason the registration has become useless or ineffective and therefore requires to be revoked. The Central Government is however, required to give an opportunity to the owner of the undertaking to be heard, before revoking the registration.

### **Licensing of Industrial Undertakings**

The major instrument of implementation of industrial policy is the system of grant of various industrial approvals such as, industrial licence, foreign collaborations, import of capital goods, etc. The system of industrial licensing helps the Government to provide and develop the industries in the country in conformity with the national objectives and priorities. As per the new Industrial Policy, 1991, licensing is required only for certain industries related to security and strategic concerns, social reasons, hazardous chemicals and overriding environmental reasons and items of elitist consumption.

#### **What is an Industrial Licence?**

*An Industrial licence is a written permission from the Government to an industrial undertaking to manufacture specified articles, listed in the First Schedule and includes particulars of industrial undertaking, its location, articles to be manufactured, the capacity on the basis of maximum utilisation of plant and machinery etc. The licence is subject to a validity period within which the licensed capacity of the undertaking should be established.*



### **Licensing of New Undertaking**

Under Section 11, no person or authority other than Central Government after the commencement of the Act, shall establish any new industrial undertaking without a licence from the Central Government. The licence may contain such conditions including in particular, the location and size of the undertaking as the Central Government may deem fit. In case any State Government wants to establish any new industrial undertaking, previous permission of the Central Government would be required.

A licence or permission under Section 11(1) may contain certain conditions as to the location of the undertaking and the minimum standards in respect of size to be provided therein as the Central Government may impose.

### **Licence for Producing or Manufacturing New Articles**

The owner of an industrial undertaking (other than Central Government) registered under Section 10, or licensed under Section 11, shall not produce or manufacture any new article unless: (a) in the case of an industrial undertaking registered under Section 10, he has obtained a licence for producing or manufacturing such new articles, and (b) in the case of an undertaking licensed under Section 11, he has had the existing licence amended in the prescribed manner.

### **Licence for Carrying on Business After the Revocation of Certificate of Registration**

Under Section 10A, the certificate of registration granted by the Central Government can be revoked under certain circumstances. Section 13(1)(b) provides that after such revocation, the owner shall not carry on the business unless a licence or permission for this purpose has been obtained from the Government

### **Licence for Carrying on Business by an Industrial Undertaking to which the Act became applicable**

There may be cases, where the Act did not originally apply to an industrial undertaking but becomes applicable after the commencement of the Act for any reason. In such cases the owner of the undertaking concerned shall not carry on the business after the expiry of three months from the date on which the provisions become so applicable unless a licence or permission as the case may be, has been obtained from the Central Government in pursuance of clause (c) of Sub-section (1) of Section 13 of the Act.

### **Licence for Change in Location**

Under Section 13(1)(e) the owner of an industrial undertaking (other than Central Government) cannot change the location of the whole or any part of a registered industrial undertaking without the Central Government's permission/licence.

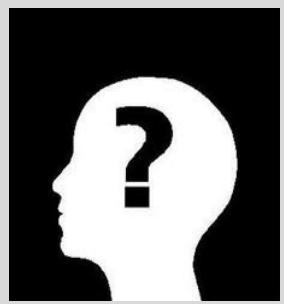
### **Licence for Effecting Substantial Expansion**

Under Section 13(1)(d), the owner of an industrial undertaking (other than Central Government) cannot effect any substantial expansion of an industrial undertaking registered or in respect of which a licence or permission has been issued, without a licence from the Central Government.

Accordingly, a licence is required for effecting any substantial expansion in any undertaking registered/licensed under the Act.

**What do you mean by the term “Substantial Expansion”?**

‘Substantial Expansion’ means the expansion of an existing industrial undertaking which substantially increases the productive capacity of the undertaking or which is of such nature as to amount virtually to a new industrial undertaking. However it does not include any such expansion as is normal to the undertaking having regard to its nature and the circumstances relating to such expansion.



Substantial increase in productive capacity would amount to substantial expansion. What is ‘productive capacity’ has, however, not been defined anywhere in the Act. Recourse should necessarily be had to the productive capacity specified in the registration certificate in terms of Section 10(5) of the Act. Again what is normal expansion in respect of that particular industrial undertaking is not to be construed as amounting to substantial expansion. This has to be determined in the context of the nature of expansion as well as the circumstances relating to such expansion. In the context of substantial expansion it should also be noted that according to the clarification of the Department of Industrial Development any increase in production by twenty five per cent over the licensed capacity being in the nature of expansion would not amount to substantial expansion if:

- no additional plant and machinery has been installed except minor balancing equipment indigenously procured;
- no additional expenditure had been incurred or foreign exchange was involved; and
- the extra production does not give rise to any additional demand for scarce raw materials.

In the context of substantial expansion, it is also relevant to note that wherever a question arises as to whether or not there has been a substantial expansion of an industrial undertaking, the decision of the Central Government thereon shall be final.

**Power of the Central Government to Revoke/Amend Licences in Certain Cases**

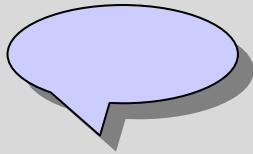
Section 12 of the Act empowers the Central Government to revoke the licence issued under Section 11 if it is satisfied, either on a reference made to it in this behalf or otherwise that the licensee has, without reasonable cause, failed to establish or to take effective steps to establish the new industrial undertaking within the prescribed time or the extended time, as the case may be.

The Central Government is also empowered under Section 12(2) to vary or amend any licence issued under Section 11. However, this power shall not be exercised when the licensee has already taken effective steps to establish the new industrial undertaking. What constitutes ‘effective steps’ has been explained earlier. As per Section 12(3), the provisions of Sections 12(1) and 12(2) shall also apply in relation to a licence issued under Section 11A of the Act (for manufacturing new article).

**INVESTIGATION****Investigation into Scheduled Industries/Industrial Undertakings**

Section 15 of the Act empowers the Central Government to cause an investigation to be made into scheduled industries or industrial undertakings.

***The Central Government may make or cause to be made a full and complete investigation into any scheduled industry or industrial undertaking, in respect of which, it is of the opinion that:***



- *there has been or is likely to be, a substantial fall in the volume of production in respect of any article or class of articles relatable to that industry or manufactured or produced in the industrial undertaking or undertakings, as the case may be, for which, having regard to the economic conditions prevailing, there is no justification; or*
- *there has been or is likely to be a marked deterioration in the quality of any article or class of articles relatable to that industry or manufactured or produced in the industrial undertaking or undertakings as the case may be, which could have been or can be avoided; or*
- *there has been or is likely to be a rise in the price of any article or class of articles relatable to that industry or manufactured or produced in the industrial undertaking or undertakings, as the case may be, for which there is no justification; or*
- *it is necessary to take any such action for the purpose of conserving any resources of national importance which are utilised in the industry or the industrial undertaking or undertakings as the case may be.*

The investigation may also be ordered by the Central Government, if it is satisfied that the industrial undertaking is being managed in a manner highly detrimental to the scheduled industry or to public interest.

In *Juggilal Kamlapat Cotton Spinning Mills v. Union of India* (1984) 3 Comp. L.J. 223 it was held that, the opinion, the Central Government is required to form before passing an order of investigation under this section is to be on a subjective satisfaction, which has to be based on relevant material. Before passing an order the party must be heard. The Central Government may either itself make an investigation or it may cause such investigation to be made by any person or body of persons appointed by it for this purpose. The scope of the investigation is wide because this section contemplates full and complete investigation. The procedure to be followed in making an investigation has been specified in the Investigation of Industrial Undertakings (Procedure) Rules, 1967. Before commencing investigation the investigator has to call upon the management of the undertaking to furnish written statements relating to the affairs thereof. He is required to probe into the causes which have brought about the above circumstances and make a report in respect of matters referred to in (i) to (iii) above after taking into account the relevant data for a period of three years. It is also required to be stated in the report that whether the opinion of the Central Government (in respect of ordering investigation) is justified and correct. The investigator is also required to give his recommendations for the purpose of taking remedial action.

### **Investigation into the Affairs of a Company in Liquidation**

Section 15A contains provisions for conducting an investigation into the affairs of a company owning an industrial undertaking.

***The prerequisites for conducting such an investigation are:***



- *the company is either being wound up by or under the supervision of a High Court;*
- *the business of such company is not being continued; and*
- *the Central Government is of the opinion that it is necessary in the interests of the general public and in particular in the interests of production, supply or distribution of articles or class of articles relatable to the scheduled industry, to investigate into the possibility of running or restarting the industrial undertaking.*

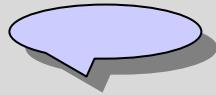
If the above circumstances are present in a particular case, the Central Government may make an application to the High Court praying for permission to make or cause to be made an investigation into possibility of re-starting or running the industrial undertaking. On application by the Central Government under this section the High Court shall, notwithstanding anything contained in the Companies Act, 1956, or in any other law for the time being in force, grant the permission prayed for.

In *Union of India v. Anglo-French Textiles Limited* [(1985) 57 Comp. Cas. 489], the Madras High Court considered the question as to whether an application filed by the Central Government seeking permission of the Court to investigate or cause any investigation to be made in regard to restarting of manufacturing unit of a company under Section 15A of the Act is maintainable even where a petition for winding up of a company under Section 433 of the Companies Act, 1956 is pending. The words used under Section 15A of the Act are the company is either being wound up by or under the supervision of a High Court. Referring to Sections 18FA(10), 18FC, 18FD, 18FE, 18FF, 18FG and 18FH, the court held that even though the application for winding up a company is pending before the Court, it can take the expression being wound up by or under the supervision of the High Court to include a case where a petition under Section 433 of the Companies Act is pending. On the other hand, the Calcutta High Court in *Union of India v. Shalimar Works Limited* 1977 47 Comp. Cas. 664 held that the expression being wound up by or under the supervision of the High Court would mean that the company is directed to be wound up, and hence the Court held that the proper stage for application under Section 15A is when the order for winding up has been made by the Court and not before that.

## **DIRECTIONS AFTER INVESTIGATION**

Section 16 of the Act provides that after investigation under Section 15, if the Central Government is satisfied that action under Section 16, is desirable, it may issue such directions to the industrial undertaking or undertakings as may be appropriate in the circumstances

***The Central Government may issue directions under Section 16 for all or any of the following purposes, namely:***



- *regulating the production of any article or class of articles by the industrial undertaking or undertakings and fixing standards of production;*
- *requiring the industrial undertaking or undertakings to take such steps as the Central Government may consider necessary to stimulate the development of the industry to which the undertaking or undertakings relates or relate;*

- *prohibiting the industrial undertaking or undertakings from resorting to any act or practice which might reduce its or their production capacity or economic value;*
- *controlling the prices, or regulating the distribution of any article or class of articles which have been the subject matter of investigation.*

Section 18 allows the person or body of persons appointed to make any investigation under Section 15 or Section 15A to choose one or more persons possessing special knowledge of any matter relating to the investigation to assist him or it in holding the investigation. Such person or body of persons so appointed have been vested with all the powers of a Civil Court under the Code of Civil Procedure, 1908 for the purpose of taking evidence on oath and enforcing the attendance of witnesses and compelling the production of documents and material objects, and the person or body of persons shall be deemed to be a Civil Court for all the purposes of Section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

### **Take-Over of Industrial Undertakings**

Chapter III-A of the Act consisting of Sections 18A, 18AA, 18B, 18C, 18D, 18E and 18F vest in the Central Government substantial powers to assume management or control of an industrial undertaking in certain cases. While Section 18A empowers the Central Government to take over an industrial undertaking whose affairs had been investigated under Section 15, Section 18AA sets out the circumstances under which the Central Government can take over an industrial undertaking without any investigation.

### **Take Over After Investigation**

Section 18A as stated above empowers the Central Government to take over the management of an industrial undertaking under certain circumstances.

Where the Central Government is of opinion that:

- (a) an industrial undertaking to which directions have been issued in pursuance of Section 16 has failed to comply with such directions; or
- (b) an industrial undertaking in respect of which an investigation has been made under Section 15 (whether or not any directions have been issued to the undertaking in pursuance of Section 16),

is being managed in a manner highly detrimental to the scheduled industry concerned or to public interest, it may, by notified order, authorise any person or body of persons to take over the management of the whole or any part of the undertaking or to exercise in respect of the whole or any part of the undertaking, such functions of control as may be specified in the order.

Such notified order shall have effect for a period not exceeding five years as may be specified in the order, but may be extended by the Central Government for a period of 2 years at a time subject to a maximum of 12 years.

### **Effect of Notified Order**

Section 18B provides that on the issue of a notified order under Section 18A authorising the taking over of the management of an industrial undertaking.

- (1) All persons in charge of the management, including persons holding office as managers or directors of the industrial undertaking immediately before the issue of notified order, shall be deemed to have vacated their office as such.

- (2) Any contract of management between the industrial undertaking and any director thereof holding office as such immediately before the issue of the notified order, shall be deemed to have terminated.
- (3) The persons or body of persons authorised under Section 18A to take over management (i) shall take all such steps as may be necessary to take into his or their custody or control all the property, effects and actionable claims to which the industrial undertaking is or appears to be entitled, and all the property and effects of the industrial undertaking shall be deemed to be in the custody of such persons from the date of the notified order; (ii) shall be for all purposes, the directors of the industrial undertaking duly constituted under the Companies Act and shall alone, be entitled to exercise all the powers of the directors of the industrial undertaking, whether such powers are derived from the said Act or from the memorandum or articles of association of the industrial undertaking or from any other source; (iii) shall take such steps as may be necessary for the purpose of efficiently managing the business of the industrial undertaking and shall exercise such other powers and have such other duties as may be prescribed; and (iv) shall, notwithstanding anything contained in the memorandum or articles of association of the industrial undertaking, exercise his or their functions in accordance with such directions as may be given by the Central Government so that they shall not have any power to give any other person any directions inconsistent with the provisions of any Act or instrument determining the functions of the authority carrying on the undertaking except in so far as may be specifically provided by the notified order.

Where any person/body of persons has been authorised to exercise any functions of control with respect to any industrial undertaking, the undertaking shall be carried on pursuant to any directions given by such authorised person(s) and any person having any function of management in relation to that undertaking shall comply with all such directions.

### Contracts in Bad Faith to be Cancelled or Varied

Section 18C provides that the persons or body of persons authorised to take over the management, may, with the previous approval of the Central Government, make an application to any court having jurisdiction in this behalf for the purpose of cancelling or varying any contract or agreement entered into any time before the issue of the notified order under Section 18A, between the industrial undertaking and any other person. The court may, after satisfying itself in this behalf that such contract or agreement had been entered into in bad faith and is detrimental to the interests of the industrial undertaking, make an order cancelling or varying that contract or agreement (either unconditionally or subject to such conditions as it may think fit) and the contract or agreement shall have effect accordingly.



*The question whether the temporary take-over of respondent company by the Central Government under Section 18A of the Act, constituted the company an instrumentality of the State and thus an authority within the meaning of Article 12 of the Constitution. The matter came for determination before the Calcutta High Court in the case of P.K. Bhattacharjee v. Indian Machinery Company Ltd. and others (1986) 3 Comp. LJ 75. The Court held that the provisions of takeover of an undertaking under Chapter IIIA of the Act did not indicate 'deep and pervasive State control so as to constitute the undertaking an instrumentality of the State. The State does not acquire ownership of the undertaking; but only for a limited period assumes management and control of the undertaking which has either failed to comply with the directions issued under Section 16 or when an industrial undertaking is being managed in a manner detrimental to the scheduled industry or to public interest. Merely because control and management had been temporarily taken over under Section 18A of the Act, it cannot be said that the undertaking was an authority within the meaning of Article 12 of the Constitution.*

Section 18D of the Act debars a person, who ceases to hold any office by reason of the above provisions, from any compensation for the loss of the office or for the premature termination of his contract of management. But the right of any such person to recover from the industrial undertaking moneys recoverable otherwise than by way of such compensation is not affected.

Section 18E of the Act provides that, notwithstanding anything contained in the Companies Act, or in the memorandum or articles of association of an undertaking taken over by the Central Government:

- (a) it shall not be lawful for the shareholders of such undertaking or any other person to nominate or appoint any person to be a director of the undertaking;
- (b) no resolution passed at any meeting of the shareholders of such undertaking shall be given effect unless approved by the Central Government;
- (c) no proceeding for the winding up of such undertaking or for the appointment of a receiver in respect thereof shall lie in any court except with the consent of the Central Government;
- (d) subject to (a), (b) and (c) above and to other provisions contained in the Act and subject to such other exceptions, restrictions, and limitations, if any, as the Central Government may, by notification in the Official Gazette, specify in this behalf, the Companies Act shall continue to apply to such undertaking in the same manner as it applied thereto before the issue of the notified order under Section 18A.

The Central Government is empowered under Section 18F to cancel any order made under Section 18A either on an application made by the owner of the industrial undertaking or otherwise, if it is satisfied that the purpose of the order under Section 18A has been fulfilled or for any other reason it is not necessary that such order should remain in force. On cancellation of such order, the management or control of the undertaking shall vest in the owner of the undertaking.

### **Take-Over without Investigation**

Section 18AA of the Industries (Development and Regulation) Act, 1951 empowers the Central Government to take over industrial undertakings without investigation under certain circumstances. Section 18AA of the Act empowers the Central Government to authorise, by a notified order, any person or body of persons to take-over the management of whole or part of any industrial undertaking and to exercise prescribed functions of control, provided the Government is satisfied on the basis of documentary or other evidences in its possession that

- the persons in charge of such industrial undertaking have, by reckless investments or creation of encumbrances on the assets of the industrial undertaking, or by diversion of funds, brought about a situation which is likely to affect the production of articles manufactured or produced in the industrial undertaking and that immediate action is necessary to prevent such a situation; or
- it has been closed for a period of not less than three months (whether by reason of the voluntary winding up of the company owning the industrial undertaking or for any other reason) and such closure is prejudicial to the concerned scheduled industry and that the financial condition of the company owning the industrial undertaking and the condition of the plant and machinery of such undertaking are such that it is possible to restart the undertaking and such restarting is necessary in the interests of the general public.

Where a notified order is made taking over an industrial undertaking, the person or body of persons, having, for the time being in charge of the management or control of the industrial undertaking, should forthwith make over the charge of management or control to the authorised person.

Such take over shall have effect for a period not exceeding five years. Where the Central Government is of the opinion that it is expedient in public interest that such notified order should continue to have effect after the expiry of the period of five years, it may from time to time issue directions for the continuance of such period, not exceeding two years at a time. However, the total period of such continuance after the initial period of five years, should not exceed twelve years.

The powers of Central Government to take over an industrial undertaking without investigation under Section 18AA does not however extend to an industrial undertaking owned by a company which is being wound up by or under the supervision of the court.

The power to take over without investigation is an extraordinary power in the hands of the Central Government and therefore, only the most extraordinary circumstances should justify the invoking of this power. Section 18AA is intended to confer power on the Central Government to enable it to take immediate steps, either as a preventive measure or in public interest without resorting to the procedure of investigation under Section 15. Action under this section can be taken only if the Central Government is satisfied with regard to the twin conditions specifically set out in the section.

Sub-section (1) of Section 18AA requires that the satisfaction of the Government in regard to the existence of the circumstances or conditions precedent, including the necessity of taking immediate action must be based on evidence in the possession of the Government. If the satisfaction of the Government in regard to the existence of any of the conditions specified in Section 18AA(1), is based on no evidence or on irrelevant evidence or on an extraneous consideration, it would vitiate the order of take over. Even where the statute conferring the discretionary power does not, in terms regulate or hedge around the formation of the opinion by the statutory authority in regard to the existence of preliminary jurisdictional facts with express checks, the authority has to form that opinion reasonably like a reasonable person. In *Swadeshi Cotton Mills v. Union of India AIR (1981) SC 818*, the Supreme Court held that in respect of such take overs without investigation, hearing at pre decisional stage must be given and the rule of *audi alterem partem* could not be dispensed with.

### Section 18A and Section 18AA - Comparison

A comparison of the provisions of Sections 18A and 18AA reveals two main points of distinction namely, (i) action under Section 18A(1)(b) can be taken only after an investigation had been made under Section 15, whereas under Section 18AA(1)(a) or (b) action can be taken without such investigation; (ii) before taking action under Section 18A(1)(b), the Central Government has to form an opinion on the basis of the investigation conducted under Section 15 in regard to the existence of the objective fact namely, that the industrial undertaking is being managed in a manner highly detrimental to the scheduled industry concerned or to public interest, whereas under Section 18AA(1)(a), the government has to satisfy itself that the persons incharge of the undertaking have brought about a situation likely to cause fall in production by committing any of the three kinds of acts specified in that provision. The phrase highly detrimental to the scheduled industry or public interest under Section 18A is capable of being construed to cover a variety of facts or things which may be considered alongwith the manner of running the industry by the management. In contrast, the action under Section 18AA can be taken if the Central Government is satisfied with regard to the existence of the twin conditions specifically mentioned therein on the basis of evidence in its possession.

### Notice Before Passing an Order under Section 18AA Whether Necessary

An important question of law arose in *Swadeshi Cotton Mills v. Union of India* (AIR 1981 S.C. 818; 1981 51 Comp. Cas. 210) as to whether the principle of natural justice of giving notice should be observed before passing an order under Section 18AA of the Act. In this case the appellant, a private company had only one

undertaking in the year 1946, mainly a textile unit at Kanpur known as the *Swadeshi Cotton Mills*, Kanpur. Between 1956 and 1973 the company set up and/or acquired 5 further textile units at Pondicherry, Naini, Udaipur, Maunath Bhanjan and Rae Bareilly. Each of these six units or undertakings of the company was separately registered in accordance with the provisions of Section 10 of the I(D&R) Act. The company made considerable progress during the years 1957 to 1973. Between 1975 and 1978 the company created encumbrances on the fixed assets. In the accounting year 1976-77 one new encumbrance was created by the company on its fixed assets.

On April 13, 1978 the Government of India in exercise of its power under Section 18AA(1)(a) of the Act, passed an order by which it authorised the National Textile Corporation Ltd. to take over the management of the whole of the said industrial undertaking subject to certain conditions. The order of take over was challenged by the company by means of writ petition filed before the Delhi High Court. The Delhi High Court rejected the petition, thereupon the company appealed against the judgement of the Delhi High Court, to the Supreme Court. The questions for consideration of Supreme Court were (1) whether it was necessary to observe the rules of natural justice before issuing a notified order under Section 18AA, or enforcing a decision under Section 18AA and (2) whether the provisions of Section 18AA and/or Section 18F impliedly excluded rules of natural justice relating to prior hearing. The appeal was allowed but without quashing the order, the case was sent back to the Central Government with the direction that it shall, within a reasonable time, preferably within three months give a full, fair and effective hearing to the aggrieved owner of the undertaking, i.e. the company on all aspects of the matter including those touching the validity and/or correctness of the impugned order and/or action of take over and then after a review of all the relevant materials and circumstances including those obtained on the date of the impugned order, shall take such fresh decision, and/or such remedial action as may be necessary, just, proper and in accordance with law.

The salient features of the judgment are given below:

The principles of natural justice consist of two basic elements, namely (i) *audi alteram partem* (Opportunity of being heard) and (ii) *nemo debet esse judex in propria causa* (Nobody should be a judge in his own cause). Irrespective of whether the power conferred on a statutory body or tribunal is administrative or quasi-judicial, a duty to act fairly, that is, in consonance with the fundamental principles of substantive justice is generally implied, because the presumption is that in a democratic polity wedded to the rule of law, the State or the Legislature does not intend that in the exercise of their statutory powers, its functionaries should act unfairly and unjustly.

It cannot be laid down as a general proposition that whenever a statute confers a power on an administrative authority and makes the exercise of that power conditional on the formation of an opinion by that authority in regard to the existence of an immediacy, its opinion in regard to that preliminary fact is not open to judicial scrutiny at all. While it may be conceded that an element of subjectivity is always involved in the formation of such an opinion, but, as was pointed out by the Supreme Court in Barium Chemicals case, the existence of the circumstances from which the inferences constituting the opinion, as the *sine qua non* for action, are to be drawn, must be demonstrable, and the existence of such circumstances, if questioned must be proved at least *prima facie*.

The expression 'immediate action' under Section 18AA(1) construed in the light of the marginal heading of the section, its context and the objects and reasons for enacting this provision only means without prior investigation under Section 15. Dispensing with the requirement of such prior investigation does not necessarily indicate an intention to exclude the application of the fundamental principles of natural justice or the duty to act fairly by affording to the owner of the undertaking likely to be affected, at the pre-decisional stage, wherever practicable, a fair hearing, adjusted, attuned and tailored to the exigency of the situation. The second reason for holding that the use of the word immediate does not necessarily and absolutely exclude the prior application of

the *audi alteram partem* rule is that immediacy or urgency requiring swift action is a situational fact having a direct nexus with the likelihood of adverse effect on fall in production. Cases of extreme urgency where action under Section 18AA(1)(a) to prevent fall in production and consequent injury to public interest, brooks absolutely no delay, would be rare. In most cases where the urgency is not so extreme, it is practicable to adjust and strike a balance between the competing claims of hurry and hearing.

The *audi alteram partem* rule is a very flexible, malleable and adaptable concept of natural justice. To adjust and harmonise the need for speed and obligation to act fairly, it can be modified and the measure of its application cut short in reasonable proportion to the exigencies of the situation. Thus in the ultimate analysis, the question (as to what extent and in what measure) this rule of fair hearing will apply at the pre-decisional stage will depend upon the degree of urgency, if any, evident from the facts and circumstances of the particular case.

The Court then found, as regards the Kanpur unit that it was closed for more than three months and there was no immediacy in relation to that unit which could absolve the government from the obligation of complying with the *audi alteram partem* rule at the pre-decisional or pre-takeover stage. As regards the other five units the court observed that the production remained fairly constant for two to three years preceding the takeover. Rather in some of the units an upward trend in production was discernible. Be that as it may, that likelihood of fall in production or adverse effect on production in these 5 units could not by any stretch of prognostication or fear of imagination, be said to be imminent, or so urgent that it could not permit the giving of even a minimal but real hearing to the company before taking over these units.

It was also observed that the power of cancellation under Section 18F can be exercised only on two grounds specified therein and these grounds and the language in which they are couched are clear enough to show that the cancellation contemplated thereunder cannot have the effect of annulling, rescinding or obliterating the order of take-over with retrospective force. It is observed that the Act did not provide any adequate remedial hearing or right of redress to the aggrieved party even where his undertaking has been arbitrarily taken over on insufficient grounds. Rather the plight of the aggrieved owner is accentuated by the provision in Section 18D which disentitles him and other person whose offices are lost or whose contract of management was terminated as a result of the takeover, from claiming any compensation whatever for such loss or termination.

The Court thus concluded that a hearing should be given to the undertaking concerned before passing an order under Section 18AA. Observance of this fundamental principle is necessary if the courts and tribunals and the administrative bodies are to command public confidence in the settlement of disputes or in taking quasi-judicial or administrative decisions affecting civil rights or legitimate interests of the citizens.

### **Take-Over of Industrial Undertaking Owned by Company in Liquidation**

Section 18FA provides that after the necessary investigations have been made under Section 15A if the Central Government is of the opinion that there are possibilities of running or restarting an industrial undertaking, and the Central Government is further satisfied that the industrial undertaking should be run for maintaining or increasing the production, supply or distribution of articles or class of articles relatable to the scheduled industry needed by the general public, it may make an application to the High Court praying for permission for appointment of any person or body of persons to take over the management or control of the whole or any part of the industrial undertaking. As soon as such an application is made by the Central Government, the High Court shall make an order empowering the Central Government to authorise any person or body of persons to take over the management of the industrial undertaking or to exercise such functions of control in relation to the whole or any part of the industrial undertaking for a period not exceeding five years. Any extension beyond this period is granted by the High Court upon an application made in this

behalf by the Central Government for a period not exceeding two years at a time. It is to be noted that the total period of extension after the expiry of the initial period of five years should not exceed twelve years.

On the High Court making an order authorising the Central Government to take over the management, the Official Liquidator (or any other person having charge of the management or control of the undertaking) shall, on the direction of the High Court make over the management of such undertaking and thereupon the authorised person shall be deemed to be the Official Liquidator in respect of the industrial undertaking. Before making over the possession of the industrial undertaking to the authorised person, the Official Liquidator shall make a complete inventory of all the assets and liabilities of the industrial undertaking in the manner specified in Section 18FG of the Act and deliver a copy of such inventory to the authorised person

On taking over the management of the industrial undertaking, the authorised person shall take immediate steps to so run the industrial undertaking as to ensure the maintenance of production. The authorised person may raise any loan for the purpose of running the industrial undertaking or the concerned part and may, for that purpose create a floating charge on the current assets of the undertaking on such terms and conditions and subject to such limitations or restrictions as may be prescribed. Where the authorised person is of opinion that the replacement or repair of any machinery of the industrial undertaking is necessary for the purpose of efficient running of the industrial undertaking he shall on such terms and conditions and subject to such limitations or restrictions as may be prescribed, make the necessary replacement or repairs. The loans obtained by the authorised person shall be recovered from the assets of the industrial undertaking in the manner prescribed. The authorised person is empowered to employ such of the former employees of the industrial undertaking whose services came to be discharged by reason of the winding up of the company and every such person employed by the authorised person shall be deemed to have entered into a fresh contract of service with the company. The proceedings in the winding up of the company in so far as they relate to the undertaking whose management has been taken over by the authorised person shall, during the period of such management or control, remain stayed and in computing the period of limitation for the enforcement of any right, privilege, obligation or liability in relation to such undertaking or the concerned part, the period during which such proceedings remain stayed shall be excluded.

### **Cancellation of the Notified Order**

Section 18F contains provisions for cancellation of the Notified Order issued under Section 18A. Section 18FD(3) further provides that the provisions of Section 18F are equally applicable to the Notified Order issued under Section 18AA and Section 18FA.

### **Preparation of Inventory of Assets and Liabilities, List of Members, etc.**

Section 18FG requires the authorised person to prepare, soon after taking over the management of an industrial undertaking of a company under Section 18A or Section 18AA or Section 18FA, a complete inventory of (a) all the properties, movable and immovable, including lands, buildings, works, workshops, stores, instruments, plant, machinery, automobiles and other vehicles, stock of materials in the course of production, storage or transit, raw materials, cash balances, cash in hand, deposits in bank or with any other person or body or on loan, reserve funds, investments and book debts and all other rights and interests arising out of such property as were immediately before the date of taking over of the industrial undertaking, in the ownership, possession, power or control of the company, whether within or without India and all books of accounts, registers, maps, property and all other documents of whatever nature relating thereto; (b) all borrowings, liabilities and obligations of whatever kind of the company including liability on account of terminal benefits to its employees subsisting immediately before the said date; and (c) a separate list of members, list of creditors of such company showing separately the secured and the unsecured creditors, as on the date of taking over of the management of the industrial undertaking.

## Power to Provide Relief to Certain Industrial Undertakings

Section 18FB of the Act contains provisions empowering the Central Government to make certain declarations in relation to an industrial undertaking, the management or control of which has been taken over under Sections 18A, 18AA or 18FA. In this context and with a view to prevent fall in the volume of production of any scheduled industry, the Government may declare, by notified order, that

- (1) all or any of the enactments mentioned in the Third Schedule to the Act shall not apply or shall apply with such adaptations whether by way of modification, addition or omission to such industrial undertakings as may be specified in the notified order. or

### ***The enactments specified in the Third Schedule are***



- *The Industrial Employment (Standing Orders) Act, 1946*
- *The Industrial Disputes Act, 1947, and*
- *The Minimum Wages Act, 1948*

- (2) the operation of all or any of the contracts, assurances, properties, agreements, settlements, awards, standing orders or other instruments in force (to which such industrial undertaking or the company owning such industrial undertaking is a party which may be applicable to such industrial undertaking or company) immediately before the date of issue of such notified order shall remain suspended or that all or any of the rights, privileges, obligations and liabilities accruing or arising thereunder before the said date, shall remain suspended or shall be enforceable by such adaptation and in such manner as may be specified in the notified order.

It should be noted that while making any modification, addition etc. in the notified order, the policy of the said enactments shall not however be affected in any way. The notified order so issued shall remain in force in the first instance for a period of one year. The duration of the notified order may be further extended by a period not exceeding one year at a time. However, no such notified order shall remain in force after the expiry of the period for which the management of the industrial undertaking was taken over under Sections 18A/18AA/18FA; or for more than 8 years in the aggregate from the date of issue of the first notified order, whichever is earlier.

A notified order issued under the provisions of Section 18FB shall be effective notwithstanding anything to the contrary contained in any other law, agreement or instrument or any decree or order of a court, tribunal, officer or other authority or of any submission, settlement or standing order. It is important to note that where the operation of certain contracts, assurances of properties, agreements, settlements, awards, etc. have been kept suspended or have been modified by the notified order, they shall remain so suspended or modified, and all the proceedings relating thereto pending before any court, tribunal, officer or other authority shall accordingly remain stayed or be continued subject to such adaptation, so that on the notified order ceasing to have effect the right, privilege, obligation, liability etc., remaining so suspended or modified shall become revived and enforceable; and any proceedings so remaining stayed shall be proceeded with from the stage at which the proceeding became stayed.

It is also provided that in computing the period of limitation for the purpose of enforcement of any right, privilege, obligation, etc. the period during which it remained suspended by virtue of the issue of the notified order under Section 18FB shall be excluded.

## Liquidation or Reconstruction of Companies

Chapter IIIAC of the Act dealing with liquidation or reconstruction of companies requires the Central

Government after the take over of management of an industrial undertaking or part thereof, to ensure that the purpose of the take over is being achieved. It is for this reason that Section 18FC of the Act confers powers on the Central Government to call upon the authorised person to submit a report on the affairs and working of the industrial undertaking whose management or control has been taken over under Sections 18A, 18AA or 18FA.

Section 18FD provides two alternatives to the Central Government in respect of receipt of the report from the authorised person. The Central Government can either decide to sell the undertaking as a running concern or it may decide to prepare a scheme for the reconstruction of the company.

The decision to sell the undertaking as a running concern may be taken by the Central Government on being satisfied that (a) in the case of the company owning the industrial undertaking, which is not being wound up by the High Court, its financial conditions and other circumstances are such that it is not in a position to meet the current liabilities out of its current assets and the interest of the general public makes it expedient to sell the undertaking as a running concern and also proceedings for winding up of the company by the High Court should be started simultaneously; (b) in the case of the undertaking concerned owned by a company and is being wound up by the High Court, its assets and liabilities are such that in the interests of its creditors and contributories, the industrial undertaking should be sold as running concern.

In terms of Section 18FD(2) the decision to prepare a scheme of reconstruction of the company owning the industrial undertaking may be ordered by the Central Government, if it is satisfied that (i) it is in the interest of the general public, or (ii) it is in the interest of the shareholders, or (iii) such a course of action is necessary to secure the proper management of the company owning the industrial undertaking. In case the scheme of reconstruction is to be prepared in relation to an undertaking owned by a company being wound up by or under the supervision of the High Court, prior permission of the High Court is to be obtained.

### **Sale of Industrial Undertaking as Running Concern**

As noted earlier, when an industrial undertaking owned by a company is taken over under section 18A, or 18AA, or 18FA, the Central Government, under section 18FD, order the sale of the said undertaking as a running company or order for the preparation of a scheme of reconstruction. Where the Government decides the course of action as specified in Section 18FD(1), namely, sale of the undertaking, then the following provisions of section 18FE would apply:

- (i) The decision of the Government to sell the undertaking as a running concern shall be deemed to be a ground specified in Section 433 of the Companies Act under which the company may be wound up by the High Court.
- (ii) The authorised person shall present an application to the High Court for winding up as soon as the decision specified in Section 18FD(1)(a) has been taken.
- (iii) Where an application has been presented as above, the High Court shall order the winding up of the company and shall appoint the authorised person as the official liquidator in relation to that undertaking.
- (iv) Where the decision to sell the undertaking as a running concern is taken under Section 18FD(1)(b), the Central Government shall cause a copy of its decision to be laid before the High Court.

Until the industrial undertaking is sold or purchased, the authorised person shall continue to function as the official liquidator and thereafter the official liquidator appointed by the Central Government under Section 448 of the Companies Act, 1956 shall take over and function as the official liquidator.

Further, it is necessary for the authorised person to report to the Central Government as to what should be

the reserve price for the sale of the industrial undertaking as a running concern. In making the report, the authorised person shall have regard to (i) the financial condition of the undertaking concerned, on the date of passing of the order under Section 18FD(1), disclosed in its books of account and as disclosed in its balance sheet and profit and loss account during a period of five years immediately preceding that date; (ii) the condition and nature of the plant, machinery, instruments and other equipment from the point of view of their suitability for profitable use in running of the industrial undertaking; (iii) the total amount of liability on account of secured and unsecured debts including overdrafts, if any, drawn on banks, liabilities on account of terminal benefits to the employees and other borrowings and liabilities of the company; and (iv) other relevant factors including the fact that the industrial undertaking will be sold free from all encumbrances.

Notice of the reserve price should be given to the members and creditors of the company to enable them to make representations to the Central Government through the authorised person. The Central Government shall after considering the representations received and the report of the authorised person, determine the reserve price. Thereafter the authorised person, with the permission of the High Court, invite tenders from the public in the manner determined by the High Court for the sale of the undertaking. The sale should be effected in favour of the highest bidder provided the price offered is not less than the reserve price. The High Court shall not refuse the permission to allow invitation to tenders if it is satisfied that the company is not in a position to meet its current liabilities out of its current assets. Where an offer equal to the reserve price is not received, the undertaking would be purchased by the Central Government at the reserve price. The amount realised from the sale of the industrial undertaking as a running concern together with any amount realised from any contributory should be utilised in accordance with the provisions of the Companies Act, 1956 in discharging its liabilities and distributing the balance, if any, to its members. In all other respects the provisions of the Companies Act, 1956 would apply relating to the winding up of the company. On sale of the undertaking, there shall be transferred to and vested in the purchaser, free from all incumbrances, all such assets existing at the time of the sale or purchase.

In case of any company in respect of which an order under Section 18FD has been made, no suit or other legal proceeding shall be instituted or continue against the company except with the previous permission of the Central Government or any officer or authority authorised by the Government in this behalf.

### **Reconstruction of the Company Owning the Industrial Undertaking**

As already stated, on receipt of the report under Section 18FC from the authorised person the Central Government has got the powers either to liquidate the company whose management has been taken over and sell the undertaking as a running concern or reconstruct the company. The power to reconstruct the company is specified in Sub-section (2) of Section 18FD. The scheme of the reconstruction may be ordered to be prepared only where the Government is satisfied that it is in the interest of the general public or it is in the interest of the shareholders or it is necessary to secure the proper management of the company owning the industrial undertaking. Section 18FF deals with certain provisions in connection with preparation of the scheme of reconstruction of the company owning the industrial undertaking the management of which has been taken over under the provisions of the Act. The Central Government as a first step shall cause to be prepared by the authorised person a scheme of reconstruction of the company containing the following:

- (a) the constitution, name and registered office, the capital, assets, powers, rights, interests, authorities and privileges, the liabilities, duties and obligations of the company on its reconstruction;
- (b) any change in the board of directors, or the appointment of a new board of directors of the company on its reconstruction and the authority by whom, the manner in which and the other terms and conditions on which such change or appointment shall be made and in the case of appointment of a new board of directors or of any director, the period for which such an appointment shall be made;

- (c) the vesting of controlling interest, in the reconstructed company in the Central Government, either by the appointment of additional directors or by the allotment of additional shares;
- (d) the alteration of the memorandum and articles of association of the company, on its reconstruction, to give effect to such reconstruction;
- (e) subject to the provisions of the scheme, the continuation by or against the company, on its reconstruction, of any action or proceedings pending against the company immediately before the date of its reconstruction;
- (f) the reduction of the interest or rights which the members and creditors have in or against the company before its reconstruction to such extent as the Central Government may consider necessary in the interests of the general public or in the interest of the members and creditors or for the maintenance of the business of the company;
- (g) the payment in cash or otherwise to the creditors in full satisfaction of their claim in respect of their interest or rights in or against the company before its reconstruction, or where their interest or rights in or against the company has or have been reduced in respect of such interest, or right as so reduced;
- (h) the allotment to the members of the company for shares held by them therein before its reconstruction [whether their interest in such shares has been reduced or not], of shares in the company on its reconstruction and where it is not possible to allot shares to any members, the payment in cash to those members in full satisfaction of their claim in respect of their interest in shares in the company before its reconstruction, or where such interest has been reduced, in respect of their interest in shares as so reduced;
- (i) the offer by the Central Government to acquire by negotiation with the members of the company their respective shares on payment in cash to those members who may volunteer to sell their shares to the Central Government in full satisfaction of their claim(i) in respect of their interest in shares in the company before its reconstruction, or (ii) where such interest has been reduced, in respect of their interest in shares as so reduced;
- (j) the conversion of any debentures issued by the company after taking over of the management of the company under Section 18A or Section 18AA or Section 18FA or of any loans obtained by the company after that date or of any part of such debentures or loans, into shares in the company and the allotment of those shares to such debentureholders or creditors, as the case may be;
- (k) the increase of the capital of the company by the issue of new shares and the allotment of such new shares to the Central Government;
- (l) the continuance of the services of such of the employees of the company as the Central Government may specify in the scheme in the company itself, on its reconstruction, on such terms and conditions as the Central Government thinks fit;
- (m) where any employees of the company whose services have been continued have, by notice in writing given to the company at any time before the expiry of one month next following the date on which the scheme is sanctioned by the High Court, intimated their intention of not becoming employees of the company, on its reconstruction, the payment to such employees and to other employees whose services have not been continued on the reconstruction of the company, of compensation, if any to which they are entitled under the Industrial Disputes Act, 1947, and such pension, gratuity, provident fund and other retirement benefits ordinarily admissible to them under the rules or authorisations of the company immediately before the date of its reconstruction;
- (n) any other terms and conditions for the reconstruction of the company;

- (o) such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction of the company shall be fully and effectively carried out.

A copy of the scheme, as approved by the Central Government shall be sent in draft to the company, to the registered trade union if any, of which the employees of the company are members and to the creditors thereof for suggestions and objections, if any, within such period as the Central Government may specify for this purpose. The Central Government may make such modifications, in the draft scheme as it may consider necessary in the light of the suggestions and objections received from the company, the registered trade union of which the employees of the company are members and any member or creditor of the company. The scheme shall thereafter be placed before the High Court for its sanction and the Court, if satisfied that the scheme is in the interests of the general public or in interests of the shareholders or for securing the proper management of the company and that the scheme is designed to be fair and reasonable to the members and creditors of the company, may, after giving a reasonable opportunity to the company and to its members and creditors of showing cause, sanction the scheme without any modification or with such modifications as it may consider necessary. The scheme sanctioned by the High Court, shall come into force on such date as the Court may specify in this behalf.

The sanction accorded by the High Court shall be conclusive evidence that all the requirements of law relating to the reconstruction of the company have been complied with. A copy of the sanctioned scheme certified by the High Court to be a true copy thereof, shall, in all legal proceedings (whether original or in appeal or otherwise), be admitted as evidence to the same extent as the original scheme. On and from the date of the coming into operation of the scheme or any provision thereof, the scheme or such provision shall be binding on the company and also on all the members and other creditors and employees of the company and on any other person having any right or liability in relation to the company. On the coming into operation of the scheme or any provision thereof, the authorised person shall cease to function, and the management of the reconstructed company shall be assumed by the Board of directors as provided in the scheme. Copies of the scheme shall be laid before each House of Parliament as soon as may be, after the scheme has been sanctioned by the Court.

### **Power to Control Supply, Distribution, Price, etc. of Certain Articles**

Chapter IIIB containing Section 18G deals with powers of the Central Government to control the supply, distribution and price, etc. of certain articles. For securing the equitable distribution and availability at fair prices of any article or class of articles relatable to any scheduled industry, the Central Government may, by notified order, provide for regulating the supply and distribution thereof and trade and commerce therein. Without prejudice to the generality of these powers, notified order made thereunder may provide for:

- controlling the prices at which any such article or class thereof may be bought or sold;
- regulating by licences, permits or otherwise the distribution, transport, disposal, acquisition, possession, use or consumption of any such article or class thereof;
- prohibiting or withholding from sale of any such article or class thereof ordinarily kept for sale;
- requiring any person manufacturing, producing or holding in stock any such article or class thereof to sell the whole or part of the articles so manufactured or produced during a specified period or to sell the whole or a part of the articles so held in stock, to such person or class of persons and in such circumstances as may be specified in the order;
- regulating or prohibiting any class of commercial or financial transactions relating to such article or class thereof which in the opinion of the authority making the order, if unregulated are likely to be detrimental to public interest;

- requiring persons engaged in the distribution and trade and commerce in any such article or class thereof to mark the articles exposed or intended for sale with the sale price or to exhibit at some easily accessible place on the premises the price-list of articles held for sale and also to similarly exhibit on the first day of every month, or at such other times as may be prescribed, a statement of the total quantities of any such articles in stock,
- collecting any information or statistics with a view to regulating or prohibiting any of the aforesaid matters; and
- any incidental or supplementary matters, including in particular, the grant or issue of licences, permits or other documents and charging of fees therefor. No such order shall be called in question in any Court.

### **General Prohibition of Taking Over Management or Control of Industrial Undertakings by State Government**

Section 20 of the Act imposes general prohibition on any State Government or a local authority to take over the management or control of any industrial undertaking under any law for the time being in force which authorises any such Government or local authority so to do.

### **Power to Exempt in Special Cases**

Under Sub-section (1) of Section 29B, the Central Government may, by notification in the Official Gazette, exempt any industrial undertaking or class of industrial undertakings or any scheduled industry or class of Scheduled Industries as may be specified, from all or any of the provisions of the Act or Rule or Order made thereunder having due regard to the smallness of the number of workers employed or the amount invested in any industrial undertaking or the desirability of encouraging small industrial undertakings generally or the stage of development of any scheduled industry and is further convinced that it would not be in public interest to apply all or any of the provisions of the Act to such undertakings.

### **Constitution of Advisory Committee**

In pursuance of Sub-section (2B) of Section 29B and in supersession of the notification of the government of India in the Ministry of Industry (Department of Industrial Policy and Promotion) Number SO 633(E), dated 12th July, 1995 the Central Government has Constituted an Advisory Committee consisting of the following persons, for giving its expert advise in the matter of determining the nature of any article or class of articles that may be reserved for production by the ancillary on small scale industrial undertakings, namely

1. Secretary to the Government of India, Ministry of Small Scale Industries and Agro and Rural Industries—Chairman.
2. Secretary to the Government of India, Department of Industrial Policy and Promotion, Ministry of Commerce and Industry—Member.
3. Advisor, Village and Small Industries Division, Planning Commission— Member.
4. Secretary to the Government of India, Department of Commerce, Ministry of Commerce and Industry—Member.
5. Additional Secretary to the Government of India and Development Commission, Small Scale Industries—Member Secretary.

The advisory Committee shall normally consider, before communicating its recommendations to the Central Government: (a) the nature of any article or class of articles which may be produced economically by ancillary or small scale undertakings; (b) the level of employment likely to be generated by the production of such article or class of articles by the ancillary or small scale undertakings; (c) the possibility of encouraging and diffusing entrepreneurship in industry; (d) the prevention of concentration of economic power to the common detriment; and (e) such other matters as it may think fit.

Under Sub-section (2A) the Central Government may, after considering the recommendations of the Advisory Committee, if satisfied that it is necessary to do so, for the development and expansion of ancillary or small scale industrial undertakings, direct by a notified order that any article or class of articles specified in the First Schedule to the Act shall, on and from such date as may be specified in the notified order be reserved for exclusive production by the small scale or ancillary industrial undertaking as the case may be.

### **Penalties**

The contravention or attempts to contravene or abetment of the contravention, by any person, of the following would be punishable under Section 24 of the Act:

1. Provisions of Section 10(1) —failure to get an existing industrial undertaking registered.
2. Provisions of Section 10(4) —failure to produce the certificate of registration issued prior to 7.2.1974 [date of coming into force of the Industries (Development and Regulation) Amendment Act, 1973] for entering therein the productive capacity.
3. Provisions of Section 11(1) —failure to obtain industrial licence for setting up a new industrial undertaking.
4. Provisions of Section 11(A) —failure to get a licence for manufacture of a new article.
5. Provisions of Section 13(1) —failure to obtain a C.O.B. licence, permission for changing location, effecting substantial expansion etc.
6. Provisions of Sub-sections (2A), (2D), (2F) and (2G) of Section 29B. [These relate to manufacture of reserved items by other than small scale units].
7. Failure to comply with the directions issued under Section 16 after an investigation.
8. Failure to comply with the directions issued under Section 18B(3) by the person/body authorised to take over the management of an industrial undertaking.
9. Any order made under Section 18G in order to control supply, distribution price etc. of certain articles.

These contraventions attract imprisonment upto six months or fine extending upto ₹5,000 or both. In case of continuing contravention, an additional fine which may extend upto ₹100 for every day of continuance of such contravention after conviction for the first such contravention, is also leviable.

If the person contravening any of the said provisions is a company, every person who at the time the offence was committed was incharge of, and was responsible to the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly. But such person shall not be liable to any punishment if he proves that the offence was committed without his knowledge or that he exercised all due diligence to

prevent the commission of such offence. Notwithstanding anything contained herein, where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of any director or manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly. The expression Company herein means any body corporate and includes a firm or other association of individuals; and director in relation to a firm, means a partner in the firm.

### **Penalty for False Statement**

Section 24A provides that, if any person(a) when required by this Act or by any order under this Act to make any statement or furnish any information, makes any statement or furnishes any information which is false in any material particular and which he knows or has reasonable cause to believe to be false or does not believe to be true; or (b) makes any such statement as aforesaid in any book, account, record, declaration, return or other document which he is required by any order made under this Act to maintain or furnish, he shall be punishable with imprisonment which may extend to three months, or with fine which may extend to two thousand rupees, or with both.

### **Cognizance of Offences**

Section 27 provides that no Court shall take cognizance of any offence punishable under this Act except on a report in writing of the facts constituting such offence made by a person who is a public servant as defined in Section 21 of the Indian Penal Code.

### **Certain Other Important Provisions**

Section 25 empowers the Central Government to delegate any of its powers under the Act (except its power under Sections 18A, 18AA and 18FA) to any officer or authority (such as the Development Council or the State Government). Where any power has been delegated to the State Government, the State Government may further delegate it to any officer or authority subordinate to it.

The Central Government has been empowered under Section 26 to issue directions to any State Government as to the execution in the State of any of the provisions of the Act or of any order or direction made thereunder.

Section 28 provides that where any person is prosecuted for contravening any order made under Section 18G which prohibits him from doing an act or being in possession of a thing without lawful authority or without a permit, licence or other document, the burden of proving that he has such authority, permit, licence or other document shall be on him.

Section 29 provides that no court inferior to that of a presidency magistrate or a magistrate of first class shall try any offence punishable under the Act.

Section 29A contains a special provision regarding fines. This section provides that notwithstanding anything contained in Section 32 of the Code of Criminal Procedure 1898 (now Cr. P.C. 1973), it shall be lawful for any magistrate of the First class and for any presidency magistrate to pass a sentence of fine exceeding one thousand rupees on any person convicted of any offence under the Act.

### **Registration and Licensing of Industrial Undertaking Rules, 1952**

The study about Industrial Licensing as contained in the Industries (Development and Regulation) Act, 1951 would be incomplete without a brief study of the provisions of Registration and Licencing of Industrial

Undertakings Rules, 1952 (RLIU Rules) which specify the procedure for making application for Registration, Industrial Licensing etc.

Under the Rules, an application for registration of an existing industrial undertaking has to be made to the Ministry of Industry, Department of Industrial Development (now Ministry of Commerce and Industry, Department of Industrial Policy & Promotion), Government of India, New Delhi, atleast 3 months before the expiry of the period fixed under Section 10(1) of the IDRA in relation to that undertaking. An application which is not made in time may be entertained by the Ministry if it is satisfied that there was sufficient cause for not making the application in time. Each application has to be accompanied by a crossed demand draft for ₹2,500 drawn on the State Bank of India, Nirman Bhawan in favour of Pay and Accounts Officer, Ministry of Commerce and Industry (Department of Industrial Policy & Promotion). On receipt of the application, the receiving officer shall note thereon the date of its receipt and send it to the applicant an acknowledgement stating the date of receipt. The Ministry or any authority appointed by it may require the applicant to furnish additional information considered necessary for the purpose of registration.

An application for the licence or permission for the establishment of a new industrial undertaking or any substantial expansion of, or the production or manufacture of any new article in, an industrial undertaking should be made before taking any of the following steps:

- (i) raising from the public any part of the capital required for the undertaking or expansion or the production or manufacture of new article;
- (ii) commencing the construction of any part of the factory building for the undertaking or expansion or the production or manufacture of new article;
- (iii) placing order for any part of the plant and machinery required for the undertaking or expansion or the production or manufacture of the new article.

An application for a licence or permission for changing the location of the whole or any part of an industrial undertaking which has been registered or in respect of which a licence or permission has been issued, should be made before: (1) Acquisition of land or the construction of premises for the purpose of housing the industrial undertaking at the proposed new site. (2) Dismantling of any part of the plant and machinery at the existing site. Each application has to be accompanied by a crossed demand draft of ₹2,500/- drawn on the State Bank of India, Nirman Bhawan, New Delhi in favour of Pay and Accounts Officer Ministry of Commerce and Industry. As in the case of an application for registration, on receipt of the application an acknowledgement would be sent to the party, and if the Ministry calls for any additional information the applicant has to furnish the same within the specified time.

Applications relating to extension of the period of validity of an industrial licence or to the issue of a carry on business licence or to diversification within the existing licensed capacity in respect of such scheduled industries as may be decided by the Government having regard to the maximisation of production, better utilisation of existing plant and machinery and other factors, could be disposed of by the Ministries concerned without reference to any Committee. Other applications would be referred to Committee constituted by the Government consisting of members drawn from the Ministries of the Central Government dealing with industries specified in the First Schedule to the IDRA, Finance, Corporate Affairs and Science and Technology and also the Planning Commission. The Committee has the power to co-opt one or more representative from the Central Government or the concerned State Government.

Where an application has been referred to the above Committee it would make an investigation and submit its report to the Ministry of Commerce and Industry for its consideration and where it decides that the licence

or permission as the case may be, should be granted it shall inform the applicant accordingly not later than three months from the date of receipt of the application or the date on which the additional information was furnished whichever is later. If the Ministry considers it essential to attach certain conditions to the licence or permission, it has to give an opportunity to the applicant to state his case. Where a licence or permission is refused, reasons therefor have to be stated.

Any owner of an industrial undertaking in respect of which a licence has been granted who desires any variance or amendment in the licence, has to apply to the Ministry of Commerce and Industry, giving reasons for such amendment.

Every owner of an industrial undertaking in respect of which a license or permission has been granted should send every half year ending on 30th June and 31st December commencing from date of grant of licence or permission as the case may be, till such time as the industrial undertaking commences production, a return in Form-G with five spare copies to the Ministry of Commerce and Industry, or any authority appointed by it. This return has to be submitted within one month after the expiry of that half year. Where any condition has been attached to a licence or permission to the effect that certain steps should be taken within a period specified therein, every owner of such industrial undertaking has to send a return in Form-G with five spare copies showing the progress made as regards the steps to be taken. This return has to be submitted within a period of 7 days from the expiry of the period specified.

If there is any change in the name of a registered industrial undertaking or an undertaking in respect of which a licence or permission has been granted, the owner thereof should, within 14 days from the date of such change, give a written notice about the change to the Ministry of Commerce and Industry forwarding also the Registration Certificates for necessary endorsement. If there is any change in the owner of a registered undertaking or an undertaking in respect of which a licence or permission has been granted, the new owner should give a written notice about the change within 14 days to the Ministry of Commerce and Industry and also forward the registration certificate for endorsing the change.

If by reason of (i) reduction in the number of workers employed; (ii) dis-continuation of the production of articles falling within the scope of the Act; or (iii) any other reason, all or any of the provisions of the Act become inapplicable to a registered industrial undertaking or an undertaking in respect of which a licence or permission has been granted, and continued to be so inapplicable for a period of six months, the owner thereof should, within a period of 14 days of the expiry of a period of six months, give notice in writing of the fact to the Ministry of Commerce and Industry. If a registered industrial undertaking or an undertaking in respect of which a licence or permission has been granted, has been closed for a period exceeding 30 days, the owner thereof shall give a notice in writing to the Ministry of Commerce and Industry within 7 days of the expiry of the period of 30 days. If any decision has been taken by a competent authority that the registered industrial undertaking or an industrial undertaking in respect of which a licence or permission has been granted shall be liquidated, the owner thereof should give a notice in writing to the Ministry of Commerce and Industry within 14 days from the date of such decision and also return the Registration Certificate or the licence.

Where a Registration Certificate or a permission granted is lost, destroyed or mutilated, a duplicate copy may be granted on receipt of a Crossed Demand Draft of ₹25 in favour of the 'Pay and Accounts Officer', Ministry of Commerce and Industry.

It may also be noted that the owner of an industrial undertaking in respect of which a licence or permission has been granted is eligible for the allotment of controlled commodities and issue of licence for import of goods required for the construction or operation or for both on preferential terms.

## **LESSON ROUND UP**

- Industrialization is a major objective of developing countries as a means to the attainment of higher levels of economic well-being of the people. Advancement of science and technology provides the wherewithal to achieve faster industrial growth.
- The object of Industries (Development and Regulation) Act is to provide to the Central Government means of implementing the Industrial Policy. It seeks to regulate the deployment of material resources of the community according to the norms laid down in the Policy and is thus an instrument for its implementation.
- An Industrial licence is a written permission from the Government to an industrial undertaking to manufacture specified articles, listed in the First Schedule and includes particulars of industrial undertaking, its location, articles to be manufactured, the capacity on the basis of maximum utilisation of plant and machinery etc.
- Industries (Development and Regulation) Act empowers the Central Government to cause an investigation to be made into scheduled industries or industrial undertakings.
- Industries (Development and Regulation) Act, 1951 empowers the Central Government to take over industrial undertakings without investigation under certain circumstances.
- The principles of natural justice consist of two basic elements, namely (i) audi alteram partem (Opportunity of being heard) and (ii) nemo debet esse judex in propria causa (Nobody should be a judge in his own cause).
- Court does not take cognizance of any offence punishable under this Act except on a report in writing of the facts constituting such offence made by a person who is a public servant as defined in Section 21 of the Indian Penal Code.

## **SELF TEST QUESTIONS**

1. Discuss in detail the objective and scope of the Industries (Development and Regulation) Act, 1951.
2. Briefly discuss the Circumstances in which the Central Government can assume management or control of an industrial undertaking.
3. What do you mean by 'New Article' under the Act?
4. What is an industrial licence? Under what circumstances an industrial licence can be revoked?
5. List out any five industries specified in First Schedule of the Act.

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# THE MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT ACT, 2006

## Section II

### LESSON OUTLINE

- Enterprise
- Micro Enterprise
- Small Enterprise
- Medium Enterprise
- Supplier
- National Board for Micro, Small and Medium Enterprises
- Functions of the Board
- Advisory Committee
- Functions of the Advisory Committee
- Memorandum of Micro, Small and Medium Enterprise
- Delayed Payment to Micro and Small Enterprise
- Facilitation Council
- Payment of Interest
- Annual Statement Accounts
- Closure of business of Micro, Small and Medium Enterprise
- Penalty for contravention
- Application for setting aside decree

### **LEARNING OBJECTIVES**

The role of Micro, Small and Medium Enterprises (MSMEs) in the economic and social development of the country is well established. In most of the developing countries like India, MSMEs play a vital role for growth of Indian economy. They play an important role in employment creation, resource utilization and income generation. The MSMEs sector is nursery of entrepreneurship, often driven by individual creativity and innovation.

In India the Micro, Small and Medium Enterprises Development Act, 2006 is the main legislation governing MSMEs. With the enactment of MSMED Act, 2006, the concept and classification of enterprises on the basis of investment were introduced.

The Company Secretaries play an important role in educating the promoters and management of the MSMEs and also perform the functions like counselling of MSMEs for the rights and benefits available to them; advisory role in formation, registration, taxation and foreign direct investment; assistance in compliance with the technicalities laid down by the MSMED Act, 2006 itself like classification of industries, registration under the Act, procedure of filing of Entrepreneurs Memorandum and disclosure requirements.

Therefore, students should be well versed in this subject so as to understand the intricacies involved in the MSMEs.

## INTRODUCTION

The role of micro, small and medium enterprises (MSMEs) in the economic and social development of the country is well established. The MSME sector is a nursery of entrepreneurship, often driven by individual creativity and innovation. This sector contributes 8 per cent of the country's GDP, 45 per cent of the manufactured output and 40 per cent of its exports. The MSMEs provide employment to about 60 million persons through 26 million enterprises. The labour to capital ratio in MSMEs and the overall growth in the MSME sector is much higher than in the large industries. The geographic distribution of the MSMEs is also more even. Thus, MSMEs are important for the national objectives of growth with equity and inclusion.

The MSME sector in India is highly heterogeneous in terms of the size of the enterprises, variety of products and services produced and the levels of technology employed. While one end of the MSME spectrum contains highly innovative and high growth enterprises, more than 94 per cent of MSMEs are unregistered, with a large number established in the informal or unorganized sector. Besides the growth potential of the sector and its critical role in the manufacturing and value chains, the heterogeneity and the unorganized nature of the Indian MSMEs are important aspects that need to be factored into policy making and programme implementation.

 *The Government has enacted the Micro, Small and Medium Enterprises Development Act, 2006 w.e.f. October 2, 2006. The Act provides for facilitating the promotion and development and enhancing the competitiveness of micro, small and medium enterprises and for matters connected therewith or incidental thereto.*

## DEFINITIONS

### Appointed Day

Section 2(b) of the Act defines the term appointed day as to mean the day following immediately after the expiry of the period of fifteen days from the day of acceptance or the day of deemed acceptance of any goods or any services by a buyer from a supplier.

### Enterprise

Section 2(c) of the Act defines the term Enterprise as an industrial undertaking or a business concern or any other establishment, by whatever name called, engaged in the manufacture or production of goods, in any manner, pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951 (IDRA) or engaged in providing or rendering of any service or services.

### Medium Enterprise

The term Medium Enterprise has been defined under Section 2(g) of the Act as to mean an enterprise classified as such under sub-clause (iii) of clause (a) or sub-clause (iii) of clause (b) of Sub-section (1) of Section 7. Section 7 deals with the classification of enterprises.

### Micro Enterprise

Micro Enterprise under Section 2(h) has been defined to mean an enterprise classified as such under sub-clause (i) of clause (a) or sub-clause (i) of clause (b) of Sub-section (1) of Section 7.

### **Small Enterprise**

Small Enterprise under Section 2(m) of the Act means an enterprise classified as such under sub-clause (ii) of clause (a) or sub-clause (ii) of clause (b) of Sub-section (1) of Section 7.

### **Supplier**

The term supplier defined under Section 2(n) of the Act means a micro or small enterprise, which has filed a memorandum with the authority referred to in Sub-section (1) of Section 8, and includes,—

- (i) the National Small Industries Corporation, being a company, registered under the Companies Act, 1956;
- (ii) the Small Industries Development Corporation of a State or a Union territory, by whatever name called, being a company registered under the Companies Act, 1956;
- (iii) any company, co-operative society, trust or a body, by whatever name called, registered or constituted under any law for the time being in force and engaged in selling goods produced by micro or small enterprises and rendering services which are provided by such enterprises.

### **NATIONAL BOARD FOR MICRO, SMALL AND MEDIUM ENTERPRISES**

Section 3 empowers the Central Government to establish National Board for Micro, Small and Medium Enterprises with its head office at Delhi and consisting of –

- (a) the Minister in charge of the Ministry or Department of the Central Government having administrative control of the micro, small and medium enterprises to be the ex officio Chairperson of the Board;
- (b) the Minister of State or a Deputy Minister, if any, in the Ministry or Department of the Central Government having administrative control of the micro, small and medium enterprises to be ex officio Vice-Chairperson of the Board. Where there is no such Minister of State or Deputy Minister, such person as may be appointed by the Central Government to be the Vice-Chairperson of the Board;
- (c) six Ministers of the State Governments having administrative control of the departments of small scale industries or, as the case may be, micro, small and medium enterprises, to be appointed by the Central Government to represent such regions of the country as may be notified by the Central Government in this behalf, ex officio;
- (d) three Members of Parliament of whom two shall be elected by the House of the People and one by the Council of States;
- (e) the Administrator of a Union territory to be appointed by the Central Government, ex officio;
- (f) the Secretary to the Government of India in charge of the Ministry or Department of the Central Government having administrative control of the micro, small and medium enterprises, ex officio;
- (g) four Secretaries to the Government of India, to represent the Ministries of the Central Government dealing with commerce and industry, finance, food processing industries, labour and planning to be appointed by the Central Government, ex officio;
- (h) the Chairman of the Board of Directors of the National Bank, ex officio;
- (i) the chairman and managing director of the Board of Directors of the Small Industries Bank, ex officio;

- (j) the chairman, Indian Banks Association, ex officio;
- (k) one officer of the Reserve Bank, not below the rank of an Executive Director to be appointed by the Central Government to represent the Reserve Bank;
- (l) twenty persons to represent the associations of micro, small and medium enterprises, including not less than three persons representing associations of women's enterprises and not less than three persons representing associations of micro enterprises, to be appointed by the Central Government;
- (m) three persons of eminence, one each from the fields of economics, industry and science and technology, not less than one of whom shall be a woman, to be appointed by the Central Government; and
- (n) two representatives of Central Trade Union Organisations, to be appointed by the Central Government; and
- (o) one officer not below the rank of Joint Secretary to the Government of India in the Ministry or Department of the Central Government having administrative control of the micro, small and medium enterprises to be appointed by the Central Government, who shall be the Member-Secretary of the Board, ex officio.

### **Functions of Board**

Section 5 empowers the Board subject to the general directions of the Central Government to, perform all or any of the following functions, namely:

- (a) examine the factors affecting the promotion and development of micro, small and medium enterprises and review the policies and programmes of the Central Government in regard to facilitating the promotion and development and enhancing the competitiveness of such enterprises and the impact thereof on such enterprises;
- (b) make recommendations on matters referred to above or on any other matter 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; and
- (c) advise the Central Government on the use of the Fund or Funds constituted under Section 12.

### **Classification of enterprises**

Section 7 empowers the Central Government to classify any class or classes of enterprises, whether proprietorship, Hindu undivided family, association of persons, co-operative society, partnership firm, company or undertaking, by whatever name called,—

- (a) in the case of the enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the IDRA as—
  - (i) a micro enterprise, where the investment in plant and machinery does not exceed twenty-five lakh rupees;
  - (ii) a small enterprise, where the investment in plant and machinery is more than twenty-five lakh rupees but does not exceed five crore rupees; or
  - (iii) a medium enterprise, where the investment in plant and machinery is more than five crore rupees but does not exceed ten crore rupees;

- (b) in the case of the enterprises engaged in providing or rendering of services, as—
- a micro enterprise, where the investment in equipment does not exceed ten lakh rupees;
  - a small enterprise, where the investment in equipment is more than ten lakh rupees but does not exceed two crore rupees; or
  - a medium enterprise, where the investment in equipment is more than two crore rupees but does not exceed five crore rupees.

It has been clarified that the cost of pollution control, research and development, industrial safety devices and such other items as may be specified shall not be included in calculating the investment in plant and machinery.

 <b>MANUFACTURING SECTOR</b>	
<b>ENTERPRISES</b>	<b>INVESTMENT IN PLANT &amp; MACHINERY</b>
MICRO ENTERPRISES	DOES NOT EXCEED TWENTY FIVE LAKH RUPEES
SMALL ENTERPRISES	MORE THAN TWENTY FIVE LAKH RUPEES BUT DOES NOT EXCEED FIVE CRORE RUPEES
MEDIUM ENTERPRISES	MORE THAN FIVE CRORE RUPEES BUT DOES NOT EXCEED TEN CRORE RUPEES

 <b>SERVICE SECTOR</b>	
<b>ENTERPRISES</b>	<b>INVESTMENT IN EQUIPMENTS</b>
MICRO ENTERPRISES	DOES NOT EXCEED TEN LAKH RUPEES
SMALL ENTERPRISES	MORE THAN TEN LAKH RUPEES BUT DOES NOT EXCEED TWO CRORE RUPEES
MEDIUM ENTERPRISES	MORE THAN TWO CRORE RUPEES BUT DOES NOT EXCEED FIVE CRORE RUPEES

### **Advisory Committee**

Section 7(2) empowers the Central Government to constitute an Advisory Committee consisting of the following members, namely:

- the Secretary of the Ministry or Department of the Central Government having administrative control of the small and medium enterprises as the Chairperson, ex officio;

- (b) not more than five officers of the Central Government possessing necessary expertise in matters relating to micro, small and medium enterprises as members, *ex officio*;
- (c) not more than three representatives of the State Governments, as members, *ex officio*; and
- (d) one representative each of the associations of micro, small and medium enterprises, as member, *ex officio*.

The Member-Secretary of the Board shall also be the *ex officio* Member-Secretary of the Advisory Committee. The Central Government has been put under obligation to obtain the recommendation of the Advisory Board before classifying any class or classes of enterprises.

### **Functions of Advisory Committee**

- (1) To examine the matters referred to it by the Board in connection with any subject referred to in Section 5 and furnish its recommendations to the Board.
- (2) To advise Central Government on any of the matters specified in Sections 9, 10, 11, 12 or 14 of Chapter IV, dealing with measures for promotion, development and enhancement of competitiveness of micro, small and medium enterprises. Section 9 deals with measures for promotion and development, Section 10 credit facilities, Section 11 procurement preference poling, Section 12 funds and Section 14 deals with administration and utilization of funds.
- (3) To advise the State Government on any of the matters specified in the rules made under Section 30. Section 30 empowers the State Government to make rules in respect of the composition of the Micro and Small Enterprises Facilitation Council, the manner of filing vacancies of the members and the procedure to be followed in the discharge of their functions by the members of the Micro and Small Enterprises facilitation Council under Sub-section (3) of Section 23.
- (4) To communicate its recommendations or advice to the Central Government or, State Government or the Board after considering the following:
  - (a) the level of employment in a class or classes of enterprises;
  - (b) the level of investments in plant and machinery or equipment in a class or classes of enterprises;
  - (c) the need of higher investment in plant and machinery or equipment for technological upgradation, employment generation and enhanced competitiveness of the class or classes of enterprises;
  - (d) the possibility of promoting and diffusing entrepreneurship in a micro, small or medium enterprise; and
  - (e) the international standards for classification of small and medium enterprises.

### **Memorandum of micro, small and medium enterprises**



*Any person who intends to establish a micro or small enterprise, may, at his discretion, or a medium enterprise engaged in providing or rendering of services may, at his discretion; or a medium enterprise engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the IDRA, is required to file the memorandum of micro, small or, as the case may be, of medium enterprise with such authority as may be specified by the State Government or the Central Government (Section 8).*

However, a person who has established before the commencement of the Act a small scale industry and obtained a registration certificate, may, at his discretion; and an industry engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to IDRA having investment in plant and machinery of more than one crore rupees but not exceeding ten crore rupees and has filed an Industrial Entrepreneur's Memorandum is required to file the memorandum with the specified authority within one hundred and eighty days from the commencement of the Act.

## **MEASURES FOR PROMOTION, DEVELOPMENT AND ENHANCEMENT OF COMPETITIVENESS**

### **Promotion and Development**

Section 9 empowers the Central Government to specify programmes, guidelines or instructions for facilitating the promotion and development and enhancing the competitiveness of micro, small and medium enterprises, particularly of the micro and small enterprises. These measures may include development of skill in the employees, management and entrepreneurs, provisioning for technological upgradation marketing assistance or infrastructure facilities and cluster development of such enterprises with a view to strengthening backward and forward linkages.

### **Credit facilities**

Section 10 stipulates that the policies and practices in respect of credit to the micro, small and medium enterprises should be progressive and such as may be specified in the guidelines or instructions issued by the Reserve Bank to ensure timely and smooth flow of credit, minimise the incidence of sickness and enhance the competitiveness of such enterprises.

### **Procurement preference policy**

With a view to facilitating promotion and development of micro and small enterprises, section 11 requires the Central Government or the State Government to notify preference policies in respect of procurement of goods and services, produced and provided by micro and small enterprises.

### **Funds**

Section 12 provides for the constitution of one or more Funds and to credit thereto any grants made by the Central Government. Section 13 obliges the Central Government to credit to the Fund or Funds by way of grants such sums of money as may be considered necessary. Section 14 empowers the Central Government to administer the Fund or Funds in the prescribed manner.

Section 14(2) stipulates that the Fund or Funds should be utilised exclusively for the specified measures. Section 14(3) casts on the Central Government the responsibility for the coordination and ensuring timely utilisation and release of sums in accordance with prescribed criteria.

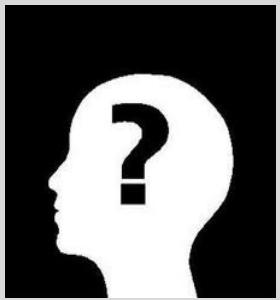
## **DELAYED PAYMENTS TO MICRO AND SMALL ENTERPRISES**

### **Liability of buyer to make payment**

Section 15 provides that where any supplier, supplies any goods or renders any services to any buyer, the buyer shall make payment therefor on or before the date agreed upon between him and the supplier in writing or, where there is no agreement in this behalf, before the appointed day. However, in no case the period agreed upon between the supplier and the buyer in writing should exceed forty-five days from the day of acceptance or the day of deemed acceptance.

**What do you mean by the day of acceptance?**

Explanation to Section 2(b) (i) of the MSMED Act, 2006 defines "the day of acceptance" as to mean the day of the actual delivery of goods or the rendering of services; or where any objection is made in writing by the buyer regarding acceptance of goods or services within fifteen days from the day of the delivery of goods or the rendering of services, the day on which such objection is removed by the supplier.



**What do you mean by the day of deemed acceptance?**

Explanation to Section 2(b) (i) of the MSMED Act, 2006 defines "the day of deemed acceptance" to mean, where no objection is made in writing by the buyer regarding acceptance of goods or services within fifteen days from the day of the delivery of goods or the rendering of services, the day of the actual delivery of goods or the rendering of services.



**Payment of Interest**

Section 16 provides that in case the buyer fails to make payment of the amount to the supplier, the buyer, notwithstanding anything contained in any agreement between the buyer and the supplier or in any law for the time being in force should pay compound interest with monthly rests to the supplier on that amount from the appointed day or, as the case may be, from the date immediately following the date agreed upon, at three times of the bank rate notified by the Reserve Bank.

**Reference to Micro and Small Enterprises Facilitation Council**

In the case of dispute regarding payment of any amount section 18 entitles any of the parties to the dispute to make a reference to the Micro and Small Enterprises Facilitation Council. The Council on receipt of a reference either itself conduct conciliation in the matter or seek the assistance of any institution or centre providing alternate dispute resolution services by making a reference to such an institution or centre, for conducting conciliation in terms of sections 65 to 81 of the Arbitration and Conciliation Act, 1996

In case the conciliation fails and stands terminated without any settlement between the parties, Section 18(3) requires the Facilitation Council either to itself take up the dispute for arbitration or refer it to any institution or centre providing alternate dispute resolution services for such arbitration in terms of the provisions of Arbitration and Conciliation Act, 1996.

Section 18(4) vests the Facilitation Council or the centre providing alternate dispute resolution services with 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. Sub-section (5) stipulates that every reference should be decided within a period of ninety days from the date of making of such a reference.

**Application for setting aside decree, award or order**

Section 19 stipulates that no application for setting aside any decree, award or other order made either by

the Facilitation Council itself or by any institution or centre providing alternate dispute resolution services to which a reference is made by the Council, shall be entertained by any court unless the appellant (not being a supplier) has deposited with it seventy-five per cent of the amount in terms of the decree, award or, as the case may be, the other order in the manner directed by such court. However, this section empowers the court pending disposal of the application to set aside the decree, award or order that such percentage of the amount deposited be paid to the supplier, as it considers reasonable under the circumstances of the case subject to such conditions as it deems necessary to impose.

### **Micro and Small Enterprises Facilitation Council**

Section 20 empowers the State Government to establish by notification, one or more Micro and Small Enterprises Facilitation Councils, at such places, exercising such jurisdiction and for such areas, as may be specified in the notification.

### **Composition of Facilitation Council**

Section 21 stipulates that the Micro and Small Enterprise Facilitation Council shall consist of not less than three but not more than five members to be appointed from among the following categories, namely:

- (i) Director of Industries, by whatever name called, 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 or, as the case may be, micro, small and medium enterprises, as chairperson; and
- (ii) one or more office-bearers or representatives of associations of micro or small industry or enterprises in the State; and
- (iii) one or more representatives of banks and financial institutions lending to micro or small enterprises; or
- (iv) one or more persons having special knowledge in the field of industry, finance, law, trade or commerce.

### **Annual statement of accounts**

Section 22 places a buyer, who is required to get his annual accounts audited under any law for the time being in force, to furnish the following additional information in his annual statement of accounts, namely:

- (i) 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;
- (ii) the amount of interest paid by the buyer in terms of section 16, along with the amounts of the payment made to the supplier beyond the appointed day during each accounting year;
- (iii) 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 as specified under the Act;
- (iv) the amount of interest accrued and remaining unpaid at the end of each accounting year; and
- (v) 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, for the purpose of disallowance as a deductible expenditure under section 23.

### **Interest not to be allowed as deduction from income**

Section 23 provides that notwithstanding anything contained in the Income-tax Act, 1961, the amount of

interest payable or paid by any buyer, under or in accordance with the provisions of the Act, shall not, for the purposes of computation of income under the Income-tax Act, 1961, be allowed as deduction.

### **Closure of business of micro, small and medium enterprises**

Section 25 places the Central Government under obligation to notify a scheme for facilitating closure of business by a micro, small or medium enterprise, not being a company registered under the Companies Act, 1956, within one year from the date of commencement of the Act.

### **Penalty for contravention**

In terms of Section 27 intentional contravention or attempting contravention or abetting the contravention of provisions of Section 8(1) relating to filing of memorandum or Section 26(2) relating to furnishing of information, has been made punishable in the case of the first conviction, with fine which may extend to rupees one thousand; and in the case of any second or subsequent conviction, with fine which shall not be less than rupees one thousand but may extend to rupees ten thousand. Contravention of the provisions of section 22, by a buyer has been made punishable with a fine which shall not be less than rupees ten thousand.

### **LESSON ROUND UP**

- The MSME Act provides for facilitating the promotion and development and enhancing the competitiveness of micro, small and medium enterprises and for matters connected therewith or incidental thereto.
- Enterprises have been classified broadly into:
  - (i) Enterprises engaged in the Manufacture/production of Goods pertaining to any industry; &
  - (ii) Enterprises engaged in providing/rendering of services.
- Manufacturing enterprises have been defined in terms of investment in plant and machinery (excluding land & buildings) and further classified into:
  - Micro Enterprises - investment up to ₹25 lakh.
  - Small Enterprises - investment above ₹25 lakh & up to ₹5 crore
  - Medium Enterprises - investment above ₹5 crore & up to ₹10 crore.
- Service enterprises have been defined in terms of their investment in equipment (excluding land & buildings) and further classified into:
  - Micro Enterprises – investment up to ₹10 lakh
  - Small Enterprises – investment above ₹10 lakh & up to ₹2 crore.
- Medium Enterprises – investment above ₹2 crore & upto ₹5 crore
- Any person who intends to establish a micro or small enterprise, may, at his discretion, or a medium enterprise engaged in providing or rendering of services may, at his discretion; or a medium enterprise engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the IDRA, is required to file the memorandum of micro, small or, as the case may be, of medium enterprise with such authority as may be specified by the State Government or the Central Government.
- Central Government under obligation to notify a scheme for facilitating closure of business by a micro, small or medium enterprise, not being a company registered under the Companies Act, 1956, within one year from the date of commencement of the Act.

## SELF TEST QUESTION

1. Define the term Enterprise under the Act?
  2. Briefly explain Micro, Small and Medium Enterprise.
  3. Explain Memorandum of micro, small and medium enterprise.
  4. Distinction between the day of acceptance and the day of deemed acceptance.
  5. Briefly explain the composition of Facilitation Council.



# Lesson 14

## LAW RELATING TO POLLUTION CONTROL AND ENVIRONMENTAL PROTECTION

### Section I

#### LESSON OUTLINE

- Concept of Sustainable Development
- Concept of Sustainable living
- Bio Diversity
- Carbon Trading
- Government Policy regarding environment
- National Conservation Strategy and Policy Statement on Environment and Development
- Environment Protection Act
- Environment
- Environment Pollutant
- Environmental Pollution
- Hazardous substance
- Power of the Central Government
- Environmental Clearance and Location of Industries
- Environmental Laboratories
- Environmental Audit
- Liability for Pollution

#### LEARNING OBJECTIVES

The term environment denotes totality of all extrinsic, physical and biotic factors affecting the life and behaviour of all living things. It is therefore important that the 'environment of which land, water, air, human beings, plants and animals are the components, be preserved and protected from degradation to enable maintenance of the ecological balance.

The concern for environmental quality has become the top most issue in the present scenario of rising population, increasing urbanization, industrial pollution, shipping, aviation and vehicular emission as well as pollution of water courses due to discharge of industrial effluents and sewage without conforming to the environmental norms and standards.

In India, as in other developing countries, the environmental problems are not confined to side affects of industrialisation but reflect the inadequacy of resources to provide infrastructural facilities to prevent industrial pollution. Other peculiar problems like population, illiteracy and unemployment obviously also pose questions regarding provisions of food, water, shelter and sanitation.

Governments National Conservation Strategy and the Policy Statement on Environment and Development is in response to the need for laying down the guidelines to help weave environmental considerations into the fabric of national life and development process. It is an expression of government's commitment for reorienting and action in unison with the environment perspective. Therefore, it is essential for the students to be familiar with the law relating to Environment Protection.

"The earth has enough resources to meet the needs of people, but will never have enough to serve their greed".

—Mahatma Gandhi

## INTRODUCTION

Advances in science and technology have, no doubt conferred many benefits on society in the form of better and improved quality of goods at comparatively reasonable prices and in comparatively large quantities. This advent of technology has also brought in its trail the problem of pollution. 'Pollution' in ordinary parlance can be defined to mean the presence of wrong matter in wrong quantity and at wrong place. For instance, storing of huge quantity of industrial gas in tanks may prove useful for production of certain articles but allowing it to escape into atmosphere may prove hazardous to the life and health of people and animals living around. Even otherwise the emissions of smoke, dust and other polluting matter from factories as a result of production process may itself pollute atmosphere which may, though not in the immediate future, in the long run be a potential source of health hazard. Therefore, it is necessary to ensure that there is sufficient checks against pollution.

Considering that these natural resources sustain life on the planet being the basis of all our activities, whether agriculture, industry, science or technology, their conservation, both quantitatively and qualitatively, is of vital importance. Protection of the environment has assumed even more importance in recent times with increased industrialization resulting not only in overdrawal of natural resources but also pollution of air, water, flora and fauna. While development is essential to every economy, it is also essential that no irreparable damage is caused to the eco-system. Hence, the approach would necessarily be that of 'sustainable development to balance the exigencies of industrial growth against the trade offs in environmental concerns.

### Concept of Sustainable Development

Universe is one of the rarest gift that the nature has given to the human being. Even after prolonged experiments the scientist could not establish, that human can survive in any other planet except earth. Therefore humanity must live within the carrying capacity of the earth. It is essential for the people who live now to use the resources of earth sustainably and prudently so that they do not deny certain benefits to future generations. Modern states use the natural resources of the earth recklessly. This will result that the Earth will not be able to support everyone unless there is less waste and extravagance. We should, therefore have, a new approach to future, that is, to secure a widespread and deeply held commitment for sustainable living. We have to integrate conservation and development, conservation to keep our actions within the earths capacity and development to enable the people everywhere to enjoy long, healthy and fulfilling lives.

The concept of 'sustainable development was first highlighted at the United Nations Conference on the Human Environment held at Stockholm in June, 1972. Since then, various countries such as Japan, US, France, Germany, etc. besides India, have enacted legislative measures for protection of the environment introducing strict penal measures for damages caused due to hazardous substances, etc. Various international conferences have been held on the subject of environmental planning etc. the recent one being the 'The United Nations Conference on Environment and Development popularly known as the Earth Summit held at Rio De Janeiro in Brazil in June, 1992 which aimed at focusing the attention of the world on problems of our environment and look for ways in which these can be avoided in future. India too has been an active participant at these conferences.

### Principles of Sustainable Living

The principles of substainable development as laid down in strategy for sustainable living, focus on respect and care for the community of life, improving the quality of human life, conserving the earths vitality and diversity, minimizing the depletion of non-renewable resources, keeping within the earths carrying capacity, changing personal attitudes and practices, enabling communities to care for their own environments,

providing a natural framework for integrating development and conservation. In addition to the above, more familiar sectors of environment and policy which requires attention are, energy, business, human settlements, fresh water, oceans and costal areas etc.

How can we achieve this? An ethic based on respect and care for each other and for Earth is the foundation of sustainable living. Development ought not to be at the expense of other groups or later generations. Development should not threaten the survival of other species. The benefits and costs of resource use and environmental conservation should be shared fairly among different communities, among people who are poor and those who are rich and between the present and the future generation.

The other aspect is the improvement of quality of human life. The aim of development is to improve the quality of human life. It should enable people to realize their potential and lead lives of dignity and fulfilment. Economic growth is part of development but it cannot be a goal in itself. Some of universally accepted goals are, healthy life, education, access to the resources needed for a decent standard of living, political freedom etc.

Most important principle of the sustainable development is to conserve the earths vitality and diversity. Development must be conservation based. It must protect the structure, functions and diversity of the worlds natural systems on which our species depends. To this end, we need to conserve life support system, conserve bio diversity and ensure that the use of renewable resources is sustainable. This object can be achieved only if the pollution is prevented. Governments should initiate preventive action by minimizing wherever possible discharges of substances that could be harmful. To use biological resources sustainably, we have to regulate the harvest system on the basis of careful study of stocks so that any over use can be corrected. Efforts should be initiated to minimize the depletion of non-renewable resources like minerals, oil, gas and coal, while these cannot be used sustainably, their life can be extended. This can be done by using less of such resource to make a particular product or by switching to renewable substitutes wherever possible. This is essential if the earth is to sustain billions of more people in future.

Scientists and environmentalists warn that there are finite limits to the carrying capacity of the earths ecosystems. The limits vary from region to region and the impacts depend on how many people are there, and how much food, water, energy and raw material each person uses and wastes. Policies that bring human numbers and life styles into balance with the earths carrying capacity must be complemented by technologies that enhances that capacity by careful management.

Information must be disseminated through formal and informal education so that actions needed are widely understood. Communities and local groups provide the earliest channels for people to express their concern and take action to create security-based sustainable societies. However, such communities need the authority, power and knowledge to act. People who organise themselves to work for sustainability in their own communities can be an effective force whether their community is rich, poor, urban, sub-urban or rural. All societies need a foundation of information and knowledge, a framework of law and institutions and consistent economic and social policies if they are to advance in a rational way.

Global sustainability depends upon a firm alliance among all countries. But levels of development in world are unequal and the lower income countries must be helped to develop sustainability and to protect their environments. The ethic of care applies at the international, national as well as individual levels. No nation is self sufficient. All tend to gain from worldwide sustainability and all are threatened if we fail to attain it.

The lower income countries must develop their industry to escape from acute poverty and achieve sustainability. We must adopt practices that build concern for the earth into the structure of business, industry and commerce, we need to introduce processes that minimize the use of raw materials and energy, reduce waste and prevent pollution.

As regard the human settlement, in all countries, changes in the city design, transport systems and resource use are essential to ensure sustainability. More people are hungry now than before, large areas are affected by land degradation resulting from misuse. The increased food requirement to meet the needs of twice as many people must come largely from better use of land already farmed.

Life on earth depends on water but water mismanagement is reducing agricultural productivity, spreading disease and endangering ecological balance. The oceans cover more than two thirds of the placement surface. The costal zones are increasingly polluted from the adjacent land that impair ecological function and reduce yield of sea products.

It is therefore high time that we have to care for the earth. The challenges we face cannot be solved overnight by some new vision. Action by governments and strengthened international institutions is of primary importance and the attitudes and practices of individuals also count as much.

### **Government Policy Regarding Environment**

The survival and well being of a nation depend on sustainable development. It is a process of social and economic betterment that satisfies the needs and values of all interest groups without foreclosing further options. In the past, we had a great tradition of environment conservation which taught us to respect nature and to take cognizance of the fact that all forms of life-human, animal and plant are closely interlinked and that disturbance in one gives rise to an imbalance in others. This principle is included in the Directive Principles in the Constitution of India. It states that States shall endeavour to protect and improve the environment and to safeguard the forests and wildlife in the country and to protect and improve the natural environment including forests, lakes and rivers and wild life and to have compassion for the living creatures.

Governments National Conservation Strategy and the Policy Statement on Environment and Development is in response to the need for laying down the guidelines to help weave environmental considerations into the fabric of national life and development process. It is an expression of governments commitment for reorienting and action in unison with the environment perspective.

### **BIO-DIVERSITY**

Biodiversity, the natural biotic capital of the earth, is fundamental to the fulfillment of human needs and vital for the survival of this planet. Biodiversity thus is life insurance for life itself. India is an identified mega diverse country, rich in biodiversity and associated traditional knowledge. India's strategy for conservation and sustainable utilization of biodiversity focuses on according special status and protection to biodiversity rich areas by declaring them as national parks, wildlife sanctuaries, biosphere reserves, and ecologically fragile and sensitive areas; diverting pressure on reserve forests by supporting alternative measures for meeting fuel wood and fodder needs of people; afforestation of degraded areas and wastelands; and creation of ex situ conservation facilities such as gene banks, within the overall ambit of a stable institutional framework.

The country also has a tradition of conservation and sustainable use of its biodiversity, which has now come under pressure on account of various factors including development imperatives, habitat fragmentation, and introduction of invasive alien species. A global scientific analysis of current trends and plausible future scenarios project that biodiversity loss is likely to continue in the foreseeable time largely because the direct drivers of biodiversity loss are projected to either remain constant or to increase in the near future. However, biodiversity is being increasingly threatened globally on account of various factors. Human activities are also placing severe pressure on biological resources, and increasingly leading to fragmentation and degradation of habitats, and resultant loss of biodiversity. These losses are irreversible and are a threat to our own well-

being. This global concern about loss of biodiversity is sought to be addressed in the international Convention on Biological Diversity (CBD), to which India is a Party.

India has participated in all major international events on environment issues, since the Stockholm Conference on Human Environment and Development in 1972. The country has contributed to and ratified several key multilateral agreements on environment issues, including the Convention on Biological Diversity (CBD). Pursuant to the CBD, following a widespread consultative process, a 'National Policy and Macrol level Action Strategy on Biodiversity' was developed in 1999 to consolidate and augment existing strategies and programmes relating to biodiversity. India has also enacted the Biological Diversity Act, 2002, which was developed through an extensive and intensive consultation process initiated in 1994. India is one of the few countries to have enacted such legislation. This Act primarily aims at giving effect to the provisions of the Convention, including regulating access to biological resources and associated traditional knowledge so as to ensure equitable sharing of benefits arising out of their use, in accordance with the provisions of Article 15 of the CBD. The Government has also promulgated the Biological Diversity Rules in 2004.

The National Environment Policy (NEP) 2006 seeks to achieve balance and harmony between conservation and development. The policy is intended to mainstream environmental concerns in all development activities. Biological diversity, or biodiversity, encompasses the variety of all life on earth. Biodiversity manifests itself at three levels: species diversity which refers to the numbers and kinds of living organisms; genetic diversity which refers to genetic variation within species; and ecosystem diversity which denotes the variety of habitats, biological communities and ecological processes.

The Biological Diversity Act 2002 was born out of India's attempt to realise the objectives enshrined in the United Nations Convention on Biological Diversity (CBD) 1992 which recognizes the sovereign rights of states to use their own Biological Resources. The Act aims at the conservation of biological resources and associated knowledge as well as facilitating access to them in a sustainable manner and through a just process.

Biological Diversity Act, 2002 provides for conservation of biological diversity, sustainable use of its components and fair and equitable sharing of the benefits arising out of the use of biological resources, knowledge and for matters connected therewith or incidental thereto.

## CARBON CREDIT

The most dangerous gases thrown out by the industrial units are carbon dioxide, methane, nitrous oxide, etc. and the major industry sources of green house gases are cement, steel, textile and fertilizer manufacturers. The groups of such gases, which are responsible for removing greenery from our planet, are known as green house gases(GHGs). Carbon credits are a key component of national and international attempts to mitigate the growth in concentration of green house gases (GHGs). One Carbon credit is equal to one ton of carbon. Carbon trading is an application of an emissions trading approach. Greenhouse gas emissions are capped and then markets are used to allocate the emissions among the group of regulated sources. The idea is to allow market mechanisms to drive industrial and commercial processes in the direction of low emissions or less "carbon intensive" approaches than are used when there is no cost to emitting carbon dioxide and other GHGs into the atmosphere. Since GHG mitigation projects generate credits, this approach can be used to finance carbon reduction schemes between trading partners and around the world. They are a part of international emission trading norms. They incentivise companies or countries that emit less carbon. The total annual emissions are capped and the market allocates a monetary value to any shortfall through trading. Businesses can exchange, buy or sell Carbon credits in international markets at the prevailing market price.

A company has two ways to reduce emissions. One, it can reduce the GHG (greenhouse gases) by adopting

new technology or improving upon the existing technology to attain the new norms for emission of gases. Or it can tie up with developing nations and help them set up new technology that is eco-friendly, thereby helping developing country or its companies 'earn' credits. India, China and some other Asian countries have the advantage because they are developing countries. Any company, factories or farm owner in India can get linked to United Nations Framework Convention on Climate Change (UNFCCC) and know the 'standard' level of carbon emission allowed for its outfit or activity. The extent to which one emitting less carbon (as per standard fixed by UNFCCC) one can get credited in a developing country. This is called carbon credit.

There are two distinct types of Carbon Credits : Carbon Offset Credits (COCs) and Carbon Reduction Credits (CRCs). Carbon Offset Credits consist of clean forms of energy production, wind, solar, hydro and biofuels. Carbon Reduction Credits consists of the collection and storage of Carbon from our atmosphere through reforestation, forestation, ocean and soil collection and storage efforts. Both approaches are recognized as effective ways to reduce the Global Carbon Emissions crisis.

The concept of carbon credits came into existence as a result of increasing awareness of the need for controlling emissions. The IPCC (Intergovernmental Panel on Climate Change) has observed that Policies that provide a real or implicit price of carbon could create incentives for producers and consumers to significantly invest in low-GHG products, technologies and processes. Such policies could include economic instruments, government funding and regulation.

India and China are likely to emerge as the biggest sellers and Europe is going to be the biggest buyers of Carbon credits. India is one of the countries that have 'credits' for emitting less carbon. India and China have surplus credit to offer to countries that have a deficit. Waste disposal units, plantation companies, chemical plants and municipal corporations can sell the carbon credits and make money.

Under Clean Development Mechanism one can cut the deal for Carbon credit. Under the UNFCCC charter any company from the development world can tie up with a company in the developing country that is a signatory to the Kyoto Protocol. These companies in developing countries must adopt newer technologies, emitting lesser gases, and save energy. Only a portion of the total earnings of Carbon credits of the company can be transferred to the company of the developed countries under CDM. There is a fixed quota on buying of credit by companies in Europe. The Kyoto Protocol's Clean Development Mechanism (CDM) enables countries to trade 'carbon credits', which can be earned by projects reducing greenhouse gas emissions

### **Environmental protection in India – Regulatory framework**

In India, as in other developing countries, the environmental problems are not confined to side affects of industrialisation but reflect the inadequacy of resources to provide infrastructural facilities to prevent industrial pollution. Other peculiar problems like population, illiteracy and unemployment obviously also pose questions regarding provisions of food, water, shelter and sanitation.

Though the Indian Penal Code, 1860 contains penal provisions for corrupting or fouling the water or spring or reservoir so as to make it less fit for the purpose for which it is ordinarily used as well as for vitiating the atmosphere so as to make it noxious to the health of any person etc. A number of other Central and State laws covering boilers, dangerous drugs, radiation, forests, etc. were enacted during the middle of the 20th century, however the legislative and administrative measures directed specifically at protection of the environment were introduced in the 1970s and 1980s.

The five-year plans and the Industrial Policies devoted attention to the orderly development of industries, conservation of forests, resources, urban and rural water supply and sanitation, health, and environment with considerable stress on development of industries in backward areas to ensure balanced regional

development though no specific attention was paid to the control of pollution problems. However, the Industrial Policy Statement of 1980 laid emphasis on pollution control, and preservation of ecological balance. The locational policy adopted by the Government also had a beneficial impact on balancing regional development and reducing environment pollution in highly industrialised areas.

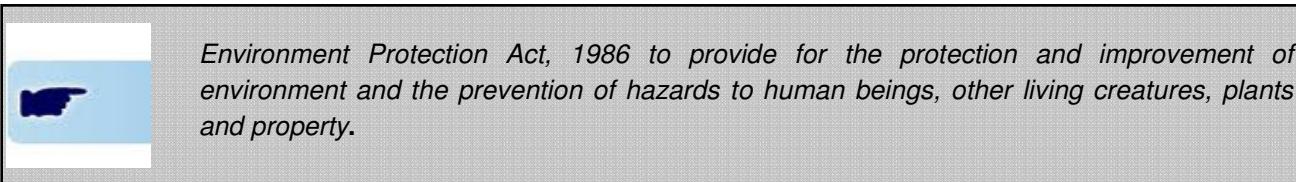
In 1972, the Department of Science and Technology set up a National Committee on Environmental Planning and Coordination to identify and investigate problems of preserving or improving the human environment and also to propose solutions for environmental problems. In 1977, by an amendment to the Constitution, Article 48A was introduced imposing a duty on the State to protect and improve the environment and safeguard the forests and wildlife of the country. Article 51A also, provides for the protection and improvement of the natural environment including forests, lakes, rivers and wild life and to have compassion for living creatures.

The Water (Prevention and Control of Pollution) Act was enacted in 1974 and the Air (Prevention and Control of Pollution) Act was passed by the Union of India in 1981, essentially to give effect to the decisions taken at the International Conference on Human Environment at Stockholm in 1972 declaring mans fundamental right to live in a pollution-free atmosphere and his responsibility to protect and improve the environment. In 1980, a Committee was set up for reviewing and recommending legislative measures and administrative machinery for ensuring environmental protection and on its recommendations, the Department of Environment was set up which became a part of the Ministry of Environment and Forests in January, 1985. This Ministry was set up mainly to act as the focal point for planning, promotion and co-ordination of environment and forestry programmes. The issues of pollution control and environment protection assumed enormous importance after the 'Bhopal Gas Tragedy in December, 1984 in which several people lost their lives or became permanently handicapped following the MIC gas leak in the Union Carbide Plant at Bhopal.

In 1986, the Government enacted the Environment Protection Act to provide for the protection and improvement of environment and the prevention of hazards to human beings, other living creatures, plants and property.

### THE ENVIRONMENT (PROTECTION) ACT, 1986

Although various legislations dealt with several environmental matters, their focus was either on specific type of pollution or on specific categories of hazardous substances, some major environmental hazards were not covered by these enactments. Moreover, control mechanisms against build up of hazardous substances and linkages in handling matters of industrial and environmental safety were inadequate. Therefore, the need was felt for a general legislation for environmental protection, to further implement the decisions of the Stockholm Conference which would inter alia, enable co-ordination of activities of the various regulatory agencies, creation of an authority or authorities with adequate powers for environmental protection, regulation of discharge of environmental pollutants and handling of hazardous substances, speedy response in the event of accidents threatening environment and deterrent punishment to those who endanger human environment, safety and health. In view of the above, the Government in 1986 enacted the Environment Protection Act.



## **Scope and Scheme of the Act**

The Act came into force on 19.11.1986 and extends to the whole of India. The Act fixes responsibility on persons carrying on industrial operations or handling hazardous substances to comply with certain safeguards for the prevention, control and abatement of environmental pollution and also enjoins upon them responsibility to furnish certain information to the authorities in certain cases. The Central Government has been granted general powers for taking all necessary measures for protecting the quality of the environment, for laying down standards for emission or discharge of environmental pollutants, and safeguards for prevention of accidents and in respect of handling hazardous substances, requiring persons to furnish certain information, issuing directions to persons, planning nationwide pollution control programmes and co-ordination of the actions of various agencies and authorities etc.

## **DEFINITIONS**

Section 2 contains definitions of various terms used in the Act. Some of the important definitions are reproduced below:

### **Environment**

In terms of Section 2(a) the definition of Environment include water, air and land and the inter-relationship which exists among and between water, air and land, and human beings, other living creatures, plants, micro-organism and property.

### **Environment pollutant**

The term Environment Pollutant has been defined under Section 2(b) as to mean any solid, liquid or gaseous substance present in such concentration as may be, or tend to be injurious to environment.

### **Environmental Pollution**

Section 2(c) defines the term Environmental Pollution, as to mean the presence in the environment of any environmental pollutant.

### **Handling**

The term Handling in relation to any substance has been defined under Section 2(d), as to mean the manufacture, processing, treatment, package, storage transportation, use, collection, destruction, conversion, offering the sale, transfer or the like of such substance.

### **Hazardous substance**

The term Hazardous Substance under Section 2(e) means any substance or preparation which, by reason of its chemical or physico-chemical properties or handling is liable to cause harm to human beings, other living creatures, micro-organism, property or the environment.

### **Occupier**

The term Occupier in relation to any factory or premises has been defined to mean a person who has control over the affairs of the factory or the premises and includes in relation to any substance, the person in possession of the substance.

### **General Powers of the Central Government**

The Central Government has been granted general powers under Section 3 to take all such measures as it

deems necessary, for protecting and improving the quality of the environment and for preventing, controlling and abating environmental pollution. Such measure include with respect to all or any of the following matters:

- (i) coordinating the actions of various State Governments, officers and authorities under this Act or rules made thereunder or under any other law concerning environmental pollution;
- (ii) planning and execution of a nation-wide programme for the prevention, control and abatement of environmental pollution;
- (iii) laying down standards for the quality of environment;
- (iv) laying down standards for emission or discharge of environmental pollutants (different standards may be laid down for different sources of emission or discharge of environmental pollutants);
- (v) restricting the carrying on of industries, operations or processes in certain areas or permitting them to be carried out subject to certain safeguards;
- (vi) laying down procedures and safeguards for the prevention of accidents which may cause environmental pollution and remedial measures for such accidents;
- (vii) laying down procedures and safeguards for the handling of hazardous substances;
- (viii) examining manufacturing processes, materials and substances as are likely to cause environmental pollution;
- (ix) carrying out and sponsoring investigations and research relating to problems of environmental pollution;
- (x) inspecting any premises, plant, equipment, machinery, manufacturing process, materials, etc. and issuing directions to any person officer or authority etc. to take steps for the prevention, control and abatement of environmental pollution;
- (xi) establishing or recognising environmental laboratories;
- (xii) collecting and disseminating information relating to environmental pollution;
- (xiii) preparing manuals, codes, guides etc. to prevent control and abate environmental pollution;
- (xiv) such other matters as the Central Government deems necessary or expedient for the purpose of securing the effective implementation of the provisions of the Act.

The Central Government is also empowered under Section 3(3) to constitute by order one or more authorities for exercising and performing such powers and functions of the Central Government as may be specified in the order.

### **Power to Appoint Officers etc.**

Section 4 empowers the Central Government to appoint officers and entrust them with certain powers and functions. The authorities and officers so constituted or appointed shall be subject to the general supervision, direction and control of the Central Government.

### **Power to Issue Directions**

In terms of Section 5 of the Act the Central Government may also, in exercise of its powers and performance of its functions, issue any directions in writing to any person, officer or authority including directions for closure, prohibition or regulation of any industry, operation or process or stoppage or regulation of the supply of electricity or water or any other service.

## Power to Make Rules

Section 6 empowers the Central Government, to make rules for all or any of the matters listed in Section 3. These rules may provide for all or any of the following matters:

- (a) the standards of quality of air, water or soil for various areas and purposes;
- (b) the maximum allowable limits of concentration of various environmental pollutants (including noise) for different areas;
- (c) the procedures and safeguards for the handling of hazardous substances;
- (d) the prohibition and restrictions on the handling of hazardous substances in different areas;
- (e) the prohibition and restrictions on the location of industries and the carrying on of processes and operations in different areas;
- (f) the procedures and safeguards for the prevention of accidents which may cause environmental pollution and for providing of remedial measures for such accident.

Section 25 also empowers the Central Government to make rules for carrying out the purpose of the Act. These rules may provide for all or any of the following matters:

- (a) the standards in excess of which environmental pollutants shall not be discharged or emitted under Section 7;
- (b) the procedure in accordance with and the safeguards in compliance with which hazardous substances shall be handled or cause to be handled under Section 8;
- (c) the authorities or agencies to which intimation of the fact of occurrence or apprehension of occurrence of the discharge of any environmental pollutant in excess of prescribed standards shall be given and to whom all assistance shall be bound to be rendered under Sub-section (1) of Section 9;
- (d) the manner in which samples of air, water, soil or other substance for the purpose of analysis shall be taken under Sub-section (1) of Section 11;
- (e) the form in which notice of intention to have a sample analysed shall be served under clause (a) of Sub-section (3) of Section 11;
- (f) the functions of the environmental laboratories, the procedure for the submission to such laboratories of samples of air, water, soil and other substances for analysis or test; the form of the laboratory report; the fees payable for such report and other matters to enable such laboratories to carry out their functions under Sub-section (2) of Section 12;
- (g) the qualifications of Government Analyst appointed or recognised for the purpose of analysis of samples of air, water, soil or other substances under Section 13;
- (h) the manner in which notice of the offence and of the intention to make a complaint to the Central Government shall be given under clause (b) of Section 19;
- (i) the authority or officers to whom any reports, returns, statistics, accounts or any other information shall be furnished under Section 20;
- (j) any other matter which is required to be, or may be, prescribed.

In exercise of its powers under Section 6 and Section 25 the Central Government has framed the Environment (Protection) Rules, 1986 vide a Notification dated November 19, 1986. The Central Government has also, in

exercise of the powers conferred on it by Sections 6, 8 and 25 of the Act, notified the following rules, viz.:

- (1) The Hazardous Wastes (Management and Handling) Rules, 1989, and
- (2) The Manufacture, Storage and Import of Hazardous Chemicals Rules, 1989.

### **Nature and Type of Regulation**

Chapter III of the Act, comprising Sections 7 to 17 contains provisions for the prevention, control and abatement of environmental pollution.

### **Standards of Emission**

Section 7 prohibits carrying on of any industry, operation or process which discharges or emits, any environmental pollutant in excess of prescribed standards.

Schedule I to the Environment Protection Rules, 1986 specifies the standards for emission or discharge of environmental pollutants. However, the Central/State Boards [constituted under Sections 3 and 4 respectively of the Water (Prevention and Control of Pollution) Act, 1974], have been empowered to prescribe more stringent standards in respect of any specific industry, operation or process. These standards are to be complied within a period of one year of being specified unless the Central/State Board has specified a lesser period or the Central Government has specified any other period in respect of any specific industry, operation or process.

In terms of Section 8 no person is authorised to handle or cause to be handled any hazardous substance except in accordance with such procedure and after complying with such safeguards as may be prescribed.

### **Obligation to Furnish Information**

Section 9 casts upon certain persons an obligation to furnish information to authorities and agencies in cases where the discharge of any environmental pollutant is in excess of the prescribed standards occurs or is apprehended to occur due to any accident or other unforeseen act or event. The person responsible for such discharge and the person in charge of the place at which such discharge occurs or is apprehended to occur are not only be bound to prevent or mitigate the environmental pollution caused as a result of such discharge but also to intimate the fact of such occurrence or apprehension of such occurrence to prescribed authorities or agencies and render all assistance to such authorities if called upon to do so. On receipt of such information, the authorities concerned are required to take the necessary remedial measures and the expenses, if any, incurred, in respect thereof may be recovered from the person concerned as arrears of land revenue or of public demand.

### **Power to Enter, Inspect, Take Samples etc.**

The powers of entry and inspection are provided under Section 10 of the Act. Accordingly any person empowered by the Central Government in this behalf has been authorised to enter at all reasonable times, any place for the purpose of

- (a) performing any of the functions entrusted to him;
- (b) determining whether and if so in what manner, any such functions are to be performed;
- (c) determining whether any of the provisions of the Act or rules make thereunder or any notice, order, directions etc. issued under the Act is being or has been complied with;
- (d) examining or testing any equipment, industrial plant, record, register document etc. or for conducting a search of any building in which an offence under this Act has been committed or

apprehended to be committed. Such a person would also have the right to seize any equipment, industrial plant, record, register, document etc. if he has reason to believe that it may furnish evidence of the commission of an offence punishable under the Act or any rules made thereunder or if he believes that such seizure is necessary to prevent or mitigate environmental pollution.

Section 10(2) obliges every person carrying on any industry, operation or process handling any hazardous substance, to render all assistance to the person empowered by the Central Government for carrying out his functions under the Act and failure to do so without any reasonable cause or excuse, renders him guilty of an offence. In terms of Section 10(3), any person willfully delaying or obstructing any person empowered under Section 10(1) in the performance of his functions, shall also be guilty of an offence.

The Central Government or any officer empowered in this behalf, is authorised under Section 11 of the Act to take, for the purpose of analysis, sample of air, water, soil or other substances from any factory, premises or other place in such manner as may be prescribed. However, the power of the person collecting samples is subject to fulfilment of following requirement:

- (i) a notice of the intention to have the sample so analysed is served on the occupier or his agent or the person in charge of place;
- (ii) the sample is collected in the presence of the occupier or his agent or the person in charge;
- (iii) the container(s) in which the sample has been placed is marked and sealed and signed both by the person taking the sample and the occupier or his agent or the person in charge;
- (iv) the samples are sent to the environmental laboratories without any delay [Section 11(3)].

However, in the event of the occupier or his agent or the person- in-charge willfully absenting himself, or being present, refuses to sign the sealed and marked containers bearing the sample, the person taking the sample may cause the container(s) to be sealed, marked and signed by him before sending it to the environmental laboratory and shall inform the Government analyst in writing, about the wilful absence of, or refusal to sign by, the occupier, his agent, or the person in charge.

The procedure for taking samples, service of notice to the occupier, his agent or the person in charge, submission of samples for analysis, and the form of the laboratory report are provided for in the Environment (Protection) Rules, 1986.

## **Environmental Laboratories**

Section 12 of the Act empowers the Central Government to establish by notification in the official Gazette, one or more environmental laboratories or recognise one or more laboratories or institutes as environmental laboratories to carry out certain functions under the Act.

## **Functions of Environmental Laboratories**

Rule 9 of the Environment (Protection) Rules, 1986 specified the following functions of environmental laboratories:

- (i) To evolve standardised methods for sampling and analysis of various types of environmental pollutants;
- (ii) To analyse samples sent by the Central Government or the Officers empowered under Sub-section (1) of Section 11;
- (iii) To carry out such investigations as may be directed by the Central Government to lay down standards for the quality of environment and discharge of environmental pollutants, to monitor and to enforce the standards laid down;

- (iv) To send periodical reports regarding its activities to the Central Government;
- (v) To carry out such other functions as may be entrusted to it by the Central Government from time to time.

These rules also specify the procedure for submission of samples to the laboratories for analysis/tests, form of the laboratory report, fees payable therefor etc.

The Central Government has also been empowered to appoint or recognise, by notification in the Official Gazette, such persons having the prescribed qualifications as Government analysts for the purpose of analysis of samples of air, water, soil or other substances sent to the environmental laboratories. The qualifications of a Government analyst have been prescribed in the Environment (Protection) Rules, 1986. As per the provisions of Section 14, any document purporting to be a report signed by a Government analyst may be used as evidence of facts in any proceeding under Act.

## OFFENCES AND PENALTIES

### Offences by Companies

Section 16 deals with offences by the companies and provides that where any offence has been committed by a company, every person who, at the time the offence was committed, was directly in charge of, and was responsible to, the company for the conduct of the business of the company, and the company itself, shall be deemed to be guilty of the offence and shall be liable to be proceeded against. When an offence has been committed by a company, and it is proved that the offence was committed with the consent or connivance of any director, manager, secretary or other officer of the company, such director, manager, secretary or other officers shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

#### ***What are the consequence if offences conducted by Government Department?***

*In the case of an offence committed by any department of the Government, the Head of the Department shall be deemed to be guilty of the offence and shall be liable to be proceeded against unless he proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence. Where it is proved that the offence committed by a Government Department has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any officer other than the Head of the Department, such officer shall also be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.*



### Penalties

Section 15 makes contravention of any of the provisions of the Act or any rules made or, orders, directions issued thereunder, punishable with imprisonment upto 5 years or with fine upto ₹1 lakh or with both. An additional fine of ₹5,000 would also be leviable for every day of continuing default. Sub-section (2) of Section 15 further provides that where such contravention continues beyond a period of one year from the date of conviction, the offender shall be punishable with imprisonment upto seven years.

## Environmental Clearance and Location of Industries

Rule 5 of the Environment Protection Rules, 1986, read with Section 3(1) and Section 3(2) empowers the Central Government to prohibit or restrict the location of industries and carrying on of processes and

operations in different areas, after taking into consideration factors, such as standards for quality of environment in an area, the maximum allowable limits of concentration of environmental pollutants (including noise) for an area, the likely emission or discharge from the proposed industry, process or operation, the topographic and climatic features of an area, the net adverse environmental impact likely to be caused by the proposed industry process, or operation, the proximity of the proposed project to protected areas and human settlements, etc.

In exercise of the powers under Sections 3(1) and 3(2)(v) of the Act and Rule 5, the Ministry of Environment and Forests has issued notifications restricting location of any industry, mining operations, cutting of trees, grazing by cattle in certain areas, construction of any clusters of dwelling units, farm houses, roads etc. and electrification in the Aravalli range (vide notification dated 9.1.1992). Any person wishing to undertake any of these operations in the said area is required to submit an application in the prescribed form along with an Environment Impact Assessment and an Environmental Management Plan. It has also been notified that the setting up of any new industrial project or the expansion or modernisation of any existing industry shall not be undertaken in any part of India unless it has been accorded environmental clearance by the Central or any State Government, as the case may be. Clearance would be so accorded only on the basis of an Environmental Impact Assessment of the project and the necessary Environmental Management Plan for the prevention, elimination or mitigation of the adverse impacts, right from the inception stage of the project. (vide notification dated 29.1.1992).

### **Requirements and Procedure for Seeking Environment Clearance of Projects**

Any person desirous to undertake any project in any part of India or the expansion or modernisation of any existing industry or project listed in Schedule I shall make an application in the prescribed proforma complete in all respect to the Secretary, Ministry of Environment and Forests, New Delhi.

### **Environmental Audit**

Rule 14 of the Environment Protection Rules, 1986 inserted w.e.f. 13.3.1992 provides for the submission of environmental audit report. Accordingly, every person carrying on an industry, operation or process requiring consent under Section 25 of the Water (Prevention and Control of Pollution) Act or Section 23 of the Air (Prevention and Control of Pollution) Act or both or authorisation under the Hazardous Wastes (Management and Handling) Rules, 1989 is required to submit an environmental audit report in Form V (inserted in the Rules) for the financial year ending on 31st March every year on or before the 15th of May, beginning 1993 to the concerned State Pollution Control Board.

### **LIABILITY FOR POLLUTION**

Liability for pollution, whether the pollution is caused by individual or by a corporation, may be civil or criminal. Civil liability refers to what is known as tortious liability. A tort is a civil wrong for which the ordinary remedy is damages. The duty breached by the wrong-doer is not one owed to any particular person but owed to all persons in general who are likely to be affected by the particular wrongful conduct. Of the various species of torts, negligence is the most directly related tort in the field of pollution. Sometimes the tort applicable in case of pollution may be that of public nuisance.

The 1861 ruling of the English Court in *Rylands v. Fletcher* provides that the person who for his own purpose brings on to his land and collects and keeps there anything likely to do mischief if it escapes must keep so at his peril and if he fails to do so, is *prima facie* liable for the damage. The liability under this rule is strict and it is no defence that the thing escaped without that persons wilful act, default or neglect or that he had no knowledge of its existence. This rule laid down the principle of liability that if a person brings on his land and collects and keeps there anything likely to do harm and such thing escaped causing damage to another, he

is liable to compensate for the damage caused. This rule applied only to non natural user of land and it did not apply to things naturally on the land or where the escape is due to an act of God, or an act of a stranger or the default of the person injured or where a thing which escapes is present by the consent of the person injured or where there is a statutory authority for doing such act.

Where liability is sought to be assigned against a person for an unintentional wrong on the basis of negligence it must be proved that the defendant owed a duty of care towards the plaintiff. Generally a person is liable only for a tort committed by himself or assisted or encouraged by him or for a tort in which he has participated. However, if an employee commits a tort within the scope of his employment, the employer also becomes liable. This vicarious liability can be attributed against a corporation also for a tort committed by its employee within the scope of its employment. If the corporation has been guilty of tortious conduct, say for example negligence in the management of a factory causing harmful pollution, can director or other officials be made liable to pay the damages for the tort? Although such extension of liability against the director etc. was not known till recently, the Supreme Courts decision in *Shri Ram Fertilisers* case is a trend setter in this direction.

The pollution laws at present, are so stringent that non-conforming factories may be asked to even close down. The laws further provide that where a State Pollution Control Board does not act in a particular case, the Central Pollution Control Board shall take suitable action in the matter. The enlargement of the powers of the Central as well as the State Board has not been all that welcome to industry. Industry circles feel that the liability under the Environment Protection Act is rather quite absolute in the sense that any person directly in charge of and responsible for conducting the affairs of the company shall be deemed to be guilty and shall be liable to be proceeded against and punished for an environmental offence, thus making a significant departure from the traditional principle of mens rea, and shifting the onus of 'no-guilt on the person concerned.

The Precursor for most stringent provisions in pollution control law is the Supreme Court judgement in *Shriram Foods and Fertilizer Industries and another v. Union of India and Others* [(1986) 1 Comp. LJ 25 (SC)]. The Supreme Court considered a writ petition seeking re-commencement of manufacturing operations in the plant especially after the manufacturing operations were ordered to be closed down because of a major leakage of oleum gas. The Supreme Court allowed the re-commencement of manufacturing operations subject to the condition that the chairman and managing director of the company and also the officers who were in actual management of the plant concerned gave an undertaking that in case there was any escape of chlorine gas resulting in death or injury to the people living in the vicinity as well as to any workman, they shall be personally liable for payment of compensation for such death or injury.

Subsequently, the Court relaxed the condition a little, by ordering that an officer who is the 'occupier of the plant under the Factories Act, 1948, and/or the officer who is responsible to the management for the actual operation of the caustic chlorine plant as its head shall be the officer who would be personally responsible to the extent of his annual salary with allowances for payment of compensation, in case of any death or injury resulting from any gas leak. The Supreme Court, however, clarified that if the escape of gas took place as a result of vis majeur or sabotage or where the officer proves that he had exercised all due diligence to prevent the escape of the gas, he shall be entitled to be indemnified by the company. The court, however, did not relax the stipulation that the chairman and managing director must be held liable to pay compensation in case of any loss or injury due to gas leak. Here also the Supreme Court clarified that there would not be any liability attached to the chairman/managing director if the gas leak was due to an act of God or vis majeur or sabotage.



*Supreme Court in M.C. Mehta and Another v. Union of India and others [(1987) 1 Comp. LJ 99 (SC)] ruled that an application for compensation in a pollution case can be maintained under Article 32 of the Constitution, for, such application is for the protection of the fundamental rights of the people and the Court has all incidental and ancillary powers including the power to forge new remedies and fashion new strategies designed to enforce fundamental rights. On the question of liability of an enterprise engaged in hazardous activities, the Supreme Court laid down for the first time a far-reaching ruling, that an enterprise which is engaged in hazardous or inherently dangerous activity and an industry which poses a potential threat to the health and safety of the persons working in the factory and of those residing in the surrounding area owes an absolute and non-delegatable duty to the community to ensure that no harm results to any one on account of an hazardous or inherently dangerous nature of the activity which it has undertaken. The Court further reiterated that the rule in Rylands v. Fletcher [(1861-73) All.E.R. 146 HL] of strict liability would apply in India but without any exceptions whatsoever recognised in England. The Court also ruled that the measure of compensation must be correlated to the magnitude and capacity of the enterprise because such compensation must have a deterrent effect.*

Subsequently the In recent times criminal liability of corporations in the sphere of pollution has also been going up. One such important case is a ruling of the Supreme Court in *U.P. Pollution Control Board v. Modi Distillery* (August 6, 1987) 8 Ind. Jud. Reports (SC) 375, in the context of the Water (Prevention and Control of Pollution) Act, 1974.

The respondent, Modi Distillery, was a company established and owned by a large business organisation known as Modi Industries Ltd. for the manufacture and sale of industrial alcohol. In the course of manufacture of industrial alcohol the industrial unit discharged its highly noxious and polluted trade effluents into a nearby river through a drain which is a stream within the meaning of Section 2(j) of the Water (Prevention and Control of Pollution) Act and thereby caused continuous pollution of the stream without the consent of the Board. Under Section 26 of the Act it is mandatory for every existing industry to obtain the consent of the Pollution Control Board for discharging trade effluents into a stream or well or sewer or on land.

The company and its industrial units applied to the Board for the grant of requisite consent to discharge the trade effluents into the stream. But on scrutiny of the application the Board found that it was incomplete in many respects. Drawing the attention of the respondent the Board asked it to make good the defects. Inspite of letters written to respondent no effort was ever made by it to rectify the defects. When the Board asked the respondent for the name of the managing director and directors and other persons responsible for the conduct of the business of the company, it did not furnish the information called for. Two subsequent letters addressed by the Board to the company did not evoke any response whereupon the Board lodged a complaint against the respondent under Section 44 of the Act in the Court of the Chief Judicial Magistrate. The respondent did not appear before the Magistrate.

In an application under Section 482 of the Cr.P.C. for quashing the proceedings, a single judge of the High Court held that no vicarious liability could be saddled on the chairman and vice-chairman and managing director and other members of the Board of directors of the company under Section 47 of the Act unless there was prosecution of the company, that is, Modi Industries Ltd.

On the question whether the chairman, vice-chairman, managing director and other members of the Board of directors were liable to be proceeded against under Section 47 of the Act in the absence of a prosecution of the company owning the industrial unit, the Supreme Court held that it is quite clear that the company did not have proper arrangement for treatment of the highly polluted trade effluents discharged by it and although the appellant Board repeatedly required the company to obtain the consent of the Board, the company was

intentionally and deliberately avoiding compliance of the requirements of Sections 25(1) and 26 of the Act. The contravention of these provisions is an offence punishable under Section 44. The chairman, vice-chairman, managing director and members of the Board of directors of Modi Industries were in charge of and responsible for the conduct of the business of the company and were therefore deemed to be guilty of the offence and liable to be proceeded against and punished under Section 47 of the Act. It would be travesty of justice if the big business house of Modi Industries Ltd. is allowed to defeat the prosecution launched and avoid facing trial on a technical flaw which is not incurable for their alleged deliberate and wilful breach of the provisions contained in Sections 25(1) and 26 made punishable under Section 44 read with Section 47 of the Act.

The Supreme Court in U.P. Pollution Control Board v. Modi Distillery (August 6, 1987) 8 Ind. Jud. Reports (SC) 375, observed that the High Court had failed to bear in mind that this situation had been brought about by the Modi Distillery of Modi Industries Ltd. because inspite of more than one notice given to it, the respondent deliberately failed to furnish the information called for. Having wilfully failed to furnish requisite information, it is now not open to the chairman and other members of the Board of directors to seek the courts assistance to derive advantage from the lapse committed by their own industrial unit.

The High Court had focussed its attention only on the technical flaw in the complaint and had failed to comprehend that the flaw had occurred due to the recalcitrant attitude of the respondent and that the infirmity was one which could be easily removed when the matter was remitted to the Chief Judicial Magistrate with a direction to call upon the appellant to make formal amendments to the averments in the complaint.

Although as a pure proposition of law in the abstract the High Courts view that there could be no vicarious liability of the chairman and others under Section 47(1) and (2) unless there was a prosecution against Modi Industries Ltd. (the company owning the industrial unit) can be termed as correct, the objection raised by the respondents in the High Court ought to have been viewed not in isolation but in the conspectus of facts and events and not in vacuum.

It is regrettable that although Parliament enacted the Water (Prevention and Control of Pollution) Act, 1974, to meet the urgent need for introducing a comprehensive legislation with its established unitary agencies in the Centre and States to provide for the prevention, abatement and the control of pollution of rivers and streams for maintaining or restoring wholesomeness of water resources and for controlling the existing and new discharges of domestic and industrial wastes, which is a matter of great national concern, the manner in which some of the Boards are functioning leaves much to be desired. This is an instance where due to the sheer negligence on the part of the legal advisors in drafting the complaint a large business house was allowed to escape the consequences of the breaches committed by it of the provisions of Act with impunity. (The error pointed out in drafting was that instead of launching prosecution against Modi Industries Ltd. the appellant Board impleaded its industrial unit Modi Distillery as respondent and this was the ground on which the High Court quashed the complaint).

### LESSON ROUND UP

- The term environment denotes totality of all extrinsic, physical and biotic factors affecting the life and behaviour of all living things. It is therefore important that the 'environment of which land, water, air, human beings, plants and animals are the components, be preserved and protected from degradation to enable maintenance of the ecological balance.
- The principles of sustainable development as laid down in strategy for sustainable living, focus on respect and care for the community of life, improving the quality of human life, conserving the earths vitality and diversity, minimizing the depletion of non-renewable resources, keeping within the earths carrying capacity, changing personal attitudes and practices, enabling communities to care for their own environments, providing a natural framework for integrating development and conservation.

- Environment Protection Act to provide for the protection and improvement of environment and the prevention of hazards to human beings, other living creatures, plants and property.
  - Environment include water, air and land and the inter-relationship which exists among and between water, air and land, and human beings, other living creatures, plants, micro-organism and property.
  - Central Government to establish by notification in the official Gazette, one or more environmental laboratories or recognise one or more laboratories or institutes as environmental laboratories to carry out certain functions under the Act.
  - Liability for pollution, whether the pollution is caused by individual or by a corporation, may be civil or criminal.

## SELF TEST QUESTIONS

1. Briefly explain the objective of Environment Protection Act, 1986?
  2. Enumerate the powers and functions of Central Government?
  3. Write short notes on sustainable development.
  4. Explain Environmental Audit.
  5. Describe functions of Environment Laboratory.

# PUBLIC LIABILITY INSURANCE ACT, 1991

## Section II

### LESSON OUTLINE

- Purpose of Public Liability Insurance Act
- Accident
- Hazardous Substance
- Handling of Hazardous Substance
- Owner
- Liability to give relief
- Compulsory Insurance
- Establishment of Environment Relief Fund
- Application for claim relief
- Award of relief
- Power of the Central Government
- Offences and Penalty
- Verification and Publication of Accident
- Power to call for information
- Power to entry and inspection

### LEARNING OBJECTIVES

The growth of hazardous industries, processes and operations in India has been accompanied by growing risks of accidents, not only to the workmen of such undertakings, but also members of the public in the vicinity. Whereas the workers are generally protected under the Workmen's Compensation Act and the Employees' State Insurance Act, members of the public who may be victims are not assured of any relief except through long-drawn legal processes. Considering that majority of the affected people belong to weaker sections of the society, and very limited resources available with them to go through legal proceedings, this Act provides for Mandatory Public Liability Insurance to be taken by companies for installations handling any hazardous substance notified under the Environment Protection Act.

Therefore, under Public Liability Insurance Act, 1991 every owner, before starting handling any hazardous substance, have to take out one or more policies to cover the liability of providing immediate relief on a specified scale to any person who suffers injury or damages to property or, in the event of death, to the legal heirs of the deceased. In this lesson, all issues relating to handling hazardous substance, liability to provide relief, compulsory insurance and other matters relating to Public Liability are discussed.

The Public Liability Insurance Act, 1991, has been enacted for providing immediate relief to the persons affected by accidents occurring while handling any hazardous substance and for other incidental and connected matters.

## INTRODUCTION

The growth of hazardous industries, processes and operations in India has been accompanied by growing risks of accidents, not only to the workmen of such undertakings, but also members of the public in the vicinity. Whereas the workers are generally protected under the Workmen's Compensation Act and the Employees' State Insurance Act, members of the public who may be victims are not assured of any relief except through long-drawn legal processes. Considering that majority of the affected people belong to weaker sections of the society, and very limited resources available with them to go through legal proceedings, this Act provides for Mandatory Public Liability Insurance to be taken by companies for installations handling any hazardous substance notified under the Environment Protection Act.

Therefore, every owner, before starting handling any hazardous substance, have to take out one or more policies to cover the liability of providing immediate relief on a specified scale to any person who suffers injury or damages to property or, in the event of death, to the legal heirs of the deceased.

Application for relief is to be made by the applicant to the Collector within 5 years of the accident, who, after giving notice to the owner and the insurer and giving the parties an opportunity of being heard, shall make the award determining the amount of relief payable. The victim will however be free to approach the Court for higher compensation.

## DEFINITIONS

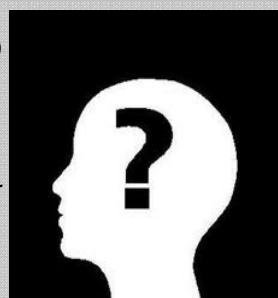
Section 2 of the Act contains definitions of the terms used in the Act. The definitions of important terms such as Accident, Hazardous Substance, Handling, and the owner, are given below:

**Accident:** Section 2(a) defines the term 'accident as to mean an accident involving a fortuitous or sudden or unintentional occurrence while handling any hazardous substance resulting in continuous, intermittent or repeated exposure to death of, or injury to, any person or damage to any property but does not include an accident by reason only of war or radio-activity.

**Hazardous Substance** has been defined under Section 2(d) and include any substance or preparation which is defined as hazardous substance under the Environment (Protection) Act, 1986 and exceeding such quantity as may be specified, by notification, by the Central Government.

**What do you mean by Hazardous Substance under Environment (Protection) Act, 1986?**

*The term Hazardous Substance under Section 2(e) Environment (Protection) Act, 1986 means any substance or preparation which, by reason of its chemical or physico-chemical properties or handling is liable to cause harm to human beings, other living creatures, micro-organism, property or the environment.*



### Electricity, whether hazardous?



*In UP Electricity Board and Another vs. District Magistrate, Dehradun and Others (AIR 1998 All LJ 1). Allahabad High Court observed that Electricity is hazardous substance covered by definition under section 2(d) of the Act. Electricity is the flow of free electrons in a particular direction at the particular moment. The flow can be any wire or even an atmosphere like lightening or in body or in other body. The electron is very small and it has been discovered by the scientist that an electron is a pins about an excess and it has got organic field. The electron is thus a material article and electricity is the flow of all these material particular in particular direction. The flow consequently is the flow of matter having physico chemical properties like when passed through water, it separate the hydrogen form the Oxygen atoms (electrolysis). Thus electricity is a substance having physico chemical process and also hazardous. Accordingly it is hazardous substance covered by definition under the Act.*

**Handling** in relation to hazardous substance has been defined under Section 2(c) to include manufacture, processing, treatment, package, storage, transportation by vehicle, use, collection, destruction, conversion, offering for sale, transfer or the like of such hazardous substance.

**Owner** under Section 2(g) means a person who owns or has control over handling any hazardous substance at the time of accident and include partners of a firm, members of an association and in the case of a company, its directors, managers, secretaries, or other officers who is directly incharge of and is responsible to, the company for the conduct of its business.

### Liability to give Relief

Section 3 of the Act incorporates the principle of liability without fault and imposes on the owner liability to give relief in case of death or injury to any person or damage to any property, resulting from an accident occurring while handling any hazardous substance. For the purposes of Section 3, injury includes permanent total or permanent partial disability or sickness resulting out of an accident.

### Compulsory Insurance

Section 4 requires the owner to take out one or more insurance policies, before starting the handling of hazardous substance. Such insurance policy should provide for contract of insurance, whereby he is insured against liability to give relief under Section 3(1) of the Act. The amount of insurance policy should not be less than the amount of paid up capital of the undertaking handling any hazardous substance and more than the amount, not exceeding rupees fifty crore, as may be prescribed.

### Verification and Publication of Accident

Section 5 of the Act requires the collector to verify, whenever it comes to his notice that an accident has occurred at any place within his jurisdiction, the occurrence of such accident and cause publicity to be given in such manner as he deems fit for inviting applications for claim for relief as provided under Section 6(1) of the Act.

### Application for Claim for Relief

Section 6 deals with manner of making application for claim for relief and provides that an application for claim for relief may be made by the person who has sustained injury; by owner of the property to which damage has been caused; and in the case of death resulting from accident, by all or any of the legal representatives of the deceased; or by any agent duly authorised by such person or owner of such property.

Every application is required to be submitted to collector in the prescribed form alongwith prescribed documents.

### **Award of Relief**

Section 7 of the Act requires the collector, on receipt of application for claim for relief, to hold an inquiry into the claim or each of the claims, after giving notice of application to owner and after giving the parties an opportunity of being heard and make an award determining the amount of relief payable to person or persons. Sub-section (3) requires the insurers to deposit, within 30 days from the date of announcement of the award, the amount in such manner as specified by the collector. The collector than arrange to pay from the relief fund to the person or persons such amount in such manner as may be specified in the scheme.

#### **Immediate – defined?**



*In Uttar Pradesh Power Corporation Ltd. & Anr. Vs. Kaliemullah & Ors (AIR 2010 Allahabad 117). Allahabad High Court (Lucknow Bench) held that if the objective of the Act is providing immediate relief is to be achieved, the mandatory public liability insurance should be on the principle of "no fault" liability as it is limited to only relief on a limited scale. However, availability of immediate relief would not prevent the victims to go to Courts for claiming larger compensation. Compensation under no fault liability may be paid by The Collector after due investigation even if no application is moved by the victim who suffered injury or is the dependant of the deceased. In case the provision contained in sub-section (1) of section 3 are interpreted otherwise with regard to award of compensation under no fault liability, then it shall frustrate the very object of the Act with regard to persons who are downtrodden, illiterate or have got no skill, knowledge or capacity to approach the authority for payment of compensation under the Act.*

### **Establishment of Environment Relief Fund**

Section 7A of the Act empowers the Central Government to establish Environment Relief Fund, by notification in the official Gazette, to be utilised for paying relief under the award made by the collector under Section 7 of the Act.

### **Power to Call for Information, Entry and Inspection etc.**

Sections 9, 10 and 11 deal with certain powers for calling for information, entry and inspection and search and seizure. The owner of hazardous installation has been put under obligation to submit to a person authorised by the Central Government such information as that person reasonably thinks necessary for the purpose of ascertaining whether any requirements of the Act, rule or directions made thereunder have been complied with. Any person, authorised by the Central Government under the provisions of Section 10 can rightfully, enter at all reasonable times with the necessary assistance, any place, premises, or vehicle where hazardous substance is handled for determining whether any provision of the Act, rule or direction made thereunder has been complied with. The owner must render all assistance to such persons.

Besides, if a person authorised by the Central Government has reason to believe that handling of any hazardous substances is taking place in any place, premises or vehicle, contravening the provisions of Section 4(1) of the Act, he may search such place, premises or vehicle, and may seize such hazardous substances, the handling of which have been found to have taken place. Such authorised person may also disposed of seized hazardous substances, if in his opinion it is expedient to prevent an accident. The expenses incurred in disposing of such hazardous substances shall be recoverable from the owner.

## Power to Give Directions

Under Section 12, the Central Government has been empowered to issue directions in writing as it may deem fit to any owner or any person, officer, authority or agency. The power of the Central Government to give directions may include the power to direct prohibition or regulation of the handling of any hazardous substance, or stoppage or regulation of the supply of electricity, water or any other service.

## Offences and Penalties

Sections 14 to 18 deal with offences, penalties and procedural provisions connected therewith. The penalties in the case of serious lapses like contravention of any provisions of Sub-section (1) or Sub-section (2) of Section 4 (not taking insurance policies), or failure to comply with any direction issued under Section 12 (in regard to prohibition or regulation of the handling of any hazardous substance or stoppage of supply of electricity, water etc.) are imprisonment for a minimum period of one year and six months but which may extend to six years, or with fine, which shall not be less than one lakh rupees or with both. For second and subsequent offences, the person shall be punishable with the minimum imprisonment of two years but which may extend to seven years and with fine which shall not be less than one lakh rupees.

Additionally lapses like default, in compliance with the directions issued under Section 9 or failure to comply with orders issued under Sub-section (2) of Section 11 or creating obstruction to any person in discharge of his duties under Section 10 or Sub-section (1) or Sub-section (3) of Section 11 shall be punishable with imprisonment which may extend to three months or with fine which may extend to rupees ten thousand or with both.

## LESSON ROUND UP

- The Public Liability Insurance Act, 1991 enacted for the purpose of providing immediate relief to the persons affected by accidents occurring while handling any hazardous substance and for other incidental and connected matters.
- Every owner, before starting handling any hazardous substance, have to take out one or more policies to cover the liability of providing immediate relief on a specified scale to any person who suffers injury or damages to property or, in the event of death, to the legal heirs of the deceased.
- Collector, on receipt of application for claim for relief, to hold an inquiry into the claim or each of the claims, after giving notice of application to owner and after giving the parties an opportunity of being heard and make an award determining the amount of relief payable to person or persons.
- Central Government to establish Environment Relief Fund, by notification in the official Gazette, to be utilised for paying relief under the award made by the collector.
- Central Government has been empowered to issue directions in writing as it may deem fit to any owner or any person, officer, authority or agency. The power of the Central Government to give directions may include the power to direct prohibition or regulation of the handling of any hazardous substance, or stoppage or regulation of the supply of electricity, water or any other service.

## SELF TEST QUESTIONS

1. Briefly explain Compulsory Insurance.
2. Enumerate the powers and functions of Central Government?
3. Write short notes on Hazardous Substance
4. Explain no fault liability.
5. Describe Compulsory Insurance Policy



# THE NATIONAL GREEN TRIBUNAL ACT, 2010

## Section III

### LESSON OUTLINE

- Environment
- Hazardous substance
- Accident
- Injury
- Substantial question relating to environment
- Establishment of the National Green Tribunal
- Composition of Tribunal
- Jurisdiction, powers and proceeding of the Tribunal
- Procedure and powers of the Tribunal
- Heads under which compensation for damage claimed
- Liability to pay relief or compensation
- Tribunal to apply certain principle
- Appeal to the Supreme Court
- Offences, penalties and procedure
- Enactments under Schedule I
- Offences by companies
- Offences by Government Department

### LEARNING OBJECTIVES

The rapid expansion in industrial, infrastructure and transportation sectors and increasing urbanisation in recent years have given rise to new pressures on our natural resources and environment. There is a commensurate increase in environment related litigation pending in various courts and other authorities. The risk to human health and environment arising out of hazardous activities has also become a matter of concern.

Taking into account the large number of environmental cases pending in higher courts. A need was felt to establish a specialised Tribunal to handle the multidisciplinary issues involved in environmental cases. Accordingly, Parliament enacted a law to provide for the establishment of the National Green Tribunal for effective and expeditious disposal of civil cases relating to environmental protection and conservation of forests and other natural resources including enforcement of any legal right relating to environment.

National Green Tribunal is a specialized body equipped with the necessary expertise to handle environmental disputes involving multidisciplinary issues. The Tribunal shall not be bound by the procedure laid down under the Code of Civil Procedure, 1908, but shall be guided by principles of natural justice. The Tribunal's dedicated jurisdiction in environmental matters shall provide speedy environmental justice and help reduce the burden of litigation in the higher Courts. Therefore, it is essential for the students to be familiar with National Green Tribunal Act, 2010.

The right to healthy environment has been construed as a part of the right to life under article 21 of the Constitution in the judicial pronouncement in India.

## INTRODUCTION

India is a party to the decisions taken at the United Nations Conference on the Human Environment held at Stockholm in June, 1972, in which India participated, calling upon the States to take appropriate steps for the protection and improvement of the human environment. The United Nations Conference on Environment and Development held at Rio de Janeiro in June, 1992, in which India participated, has also called upon the States to provide effective access to judicial and administrative proceedings, including redress and remedy, and to develop National laws regarding liability and compensation for the victims of pollution and other environmental damage. The right to healthy environment has been construed as a part of the right to life under article 21 of the Constitution in the judicial pronouncement in India.

The National Environment Tribunal Act, 1995 was enacted to provide for strict liability for damages arising out of any accident occurring while handling any hazardous substance and for the establishment of a National Environment Tribunal for effective and expeditious disposal of cases arising from such accident, with a view to giving relief and compensation for damages to persons, property and the environment. However, the National Environment Tribunal, which had a very limited mandate, was not established. The National Environment Appellate Authority Act, 1997 was enacted to establish the National Environment Appellate Authority to hear appeals with respect to restriction of areas in which any industries, operations or processes or class of industries, operations or processes shall not be carried out or shall be carried out subject to certain safeguards under the Environment (Protection) Act, 1986. The National Environment Appellate Authority has a limited workload because of the narrow scope of its jurisdiction.

The Central Government has enacted the National Green Tribunal Act, 2010 thereby repealing National Environment Tribunal Act, 1995 and National Environment Appellate Authority Act, 1997.

*The National Green Tribunal Act, 2010 intend to provide for the establishment of a National Green Tribunal for the effective and expeditious disposal of cases relating to environmental protection and conservation of forests and other natural resources including enforcement of any legal right relating to environment and giving relief and compensation for damages to persons and property and for matters connected therewith or incidental thereto.*

## DEFINITION

Section 2 contains definitions of various terms used in the Act. Some of the important definitions are reproduced below:

### **“Accident”**

According to clause (a) of Section 2 the term "accident" means an accident involving a fortuitous or sudden or unintended occurrence while handling any hazardous substance or equipment, or plant, or vehicle resulting in continuous or intermittent or repeated exposure to death, of, or, injury to, any person or damage to any property or environment but does not include an accident by reason only of war or civil disturbance.

### **“Chairperson”**

According to clause (b) of Section 2 the term "Chairperson" means the Chairperson of the National Green Tribunal.

**"Environment"**

Clause (c) Section 2 defines "environment" to includes water, air and land and the inter-relationship, which exists among and between water, air and land and human beings, other living creatures, plants, micro-organism and property.

**"Handling"**

As per Section 2(e) "handling", in relation to any hazardous substance, means the manufacture, processing, treatment, package, storage, transportation, use, collection, destruction, conversion, offering for sale, transfer or the like of such hazardous substance.

**"Hazardous substance"**

Clause (f) Section 2 defines "hazardous substance" as to means any substance or preparation which is defined as hazardous substance in the Environment (Protection) Act, 1986, and exceeding such quantity as specified or may be specified by the Central Government under the Public Liability Insurance Act, 1991.

**"Injury"**

Clause (g) Section 2 defines "injury" to include permanent, partial or total disablement or sickness resulting out of an accident.

**"Person"**

As per Section 2(j) the term "person" includes—

- (i) an individual,
- (ii) a Hindu undivided family
- (iii) a company,
- (iv) a firm,
- (v) an association of persons or a body of individuals, whether incorporated or not,
- (vi) trustee of a trust,
- (vii) a local authority, and
- (viii) every artificial juridical person, not falling within any of the preceding sub-clauses.

**"Substantial question relating to environment"**

According to clause (m) of Section 2 the term "substantial question relating to environment" shall include an instance where,—

- (i) there is a direct violation of a specific statutory environmental obligation by a person by which,—
  - (A) the community at large other than an individual or group of individuals is affected or likely to be affected by the environmental consequences; or
  - (B) the gravity of damage to the environment or property is substantial; or
  - (C) the damage to public health is broadly measurable;
- (ii) the environmental consequences relate to a specific activity or a point source of pollution.

**"Tribunal"**

According to clause (n) of Section 2 the term "Tribunal" means the National Green Tribunal established under section 3.

## ESTABLISHMENT OF THE TRIBUNAL

Section 3 of the Act empowers the Central Government, by issue of notification, to establish, a Tribunal to be known as the National Green Tribunal to exercise the jurisdiction, powers and authority conferred on such Tribunal by or under the National Green Tribunal Act, 2010.

## COMPOSITION OF THE TRIBUNAL

The Tribunal shall consist of a full time Chairperson; and not less than ten but subject to maximum of twenty full time Judicial Members as the Central Government may, from time to time, notify; and not less than ten but subject to maximum of twenty full time Expert Members, as the Central Government may, from time to time, notify.

The Chairperson of the Tribunal may, if considered necessary, invite any one or more person having specialised knowledge and experience in a particular case before the Tribunal to assist the Tribunal in that case.

The Central Government may, in consultation with the Chairperson of the Tribunal, make rules regulating generally the practices and procedure of the Tribunal including—

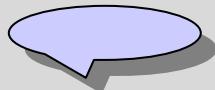
- (a) the rules as to the persons who shall be entitled to appear before the Tribunal;
- (b) the rules as to the procedure for hearing applications and appeals and other matters [including the circuit procedure for hearing at a place other than the ordinary place of its sitting falling within the jurisdiction of the Tribunal], pertaining to the applications and appeals;
- (c) the minimum number of Members who shall hear the applications and appeals in respect of any class or classes of applications and appeals:  
Provided that the number of Expert Members shall, in hearing an application or appeal, be equal to the number of Judicial Members hearing such application or appeal;
- (d) rules relating to transfer of cases by the Chairperson from one place of sitting (including the ordinary place of sitting) to other place of sitting.

## JURISDICTION, POWERS AND PROCEEDINGS OF THE TRIBUNAL

### Tribunal to Settle Dispute

Chapter III of the Act deals with jurisdiction, power and proceeding of the Tribunal. Sub section (1) of Section 14 provides that the Tribunal shall have the jurisdiction over all civil cases where a substantial question relating to environment (including enforcement of any legal right relating to environment), is involved and such question arises out of the implementation of the enactments specified in Schedule I to the Act.

#### ***Schedule I specifies following enactments:***



- (1) *The Water (Prevention and Control of Pollution) Act, 1974;*
- (2) *The Water (Prevention and Control of Pollution) Cess Act, 1977;*
- (3) *The Forest (Conservation) Act, 1980;*
- (4) *The Air (Prevention and Control of Pollution) Act, 1981;*
- (5) *The Environment (Protection) Act, 1986;*
- (6) *The Public Liability Insurance Act, 1991*
- (7) *The Biological Diversity Act, 2002,*

## Relief, Compensation and Reconstitution

Sub-section (1) of section 15 empower the Tribunal, by an order, to provide,—

- (a) relief and compensation to the victims of pollution and other environmental damage arising under the enactments specified in the Schedule I(including accident occurring while handling any hazardous substance);
- (b) for restitution of property damaged;
- (c) for restitution of the environment for such area or areas, as the Tribunal may think fit.

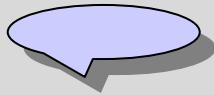
Sub-section (2) prescribes that the relief and compensation and restitution of property and environment referred to in clauses (a), (b) and (c) of sub-section (1) shall be in addition to the relief paid or payable under the Public Liability Insurance Act, 1991.

No application for grant of any compensation or relief or restitution of property or environment shall be entertained by the Tribunal unless it is made within a period of five years from the date on which the cause for such compensation or relief first arose. However, the Tribunal may, if it is satisfied that the applicant was prevented by sufficient cause from filing the application within the said period, allow it to be filed within a further period not exceeding sixty days.

The Tribunal may, having regard to the damage to public health, property and environment, divide the compensation or relief payable under separate heads specified in Schedule II so as to provide compensation or relief to the claimants and for restitution of the damaged property or environment, as it may think fit. Every claimant of the compensation or relief under the Act shall intimate to the Tribunal about the application filed to, or, as the case may be, compensation or relief received from, any other court or authority.

### Heads under which Compensation or Relief for Damages may be claimed.

***The Schedule II to the Act lists out the following heads under which compensation for damages may be claimed:***



- (a) Death;
- (b) Permanent, temporary, total or partial disability or other injury or sickness;
- (c) Loss of wages due to total or partial disability or permanent or temporary disability;
- (d) Medical expenses incurred for treatment of injuries or sickness;
- (e) Damage to private property;
- (f) Expenses incurred by the Government or any local authority in providing relief, aid and rehabilitation to the affected persons;
- (g) Expenses incurred by Government for any administrative or legal action or to cope with any harm or damage, including compensation for environmental degradation and restoration of the quality of environment;
- (h) Loss to Government or local authority arising out of, or connected with, the activity causing any damage;
- (i) Claims on account of any harm, damage or destruction to the fauna including milch and draught animals and aquatic fauna;

- (j) *Claims on account of any harm, damage or destruction to flora including aquatic flora, crops, vegetables, trees and orchards;*
- (k) *Claim including cost of restoration on account of any harm or damage to environment including pollution of soil, air, water, land and eco-system;*
- (l) *Loss and destruction of any property other than private property;*
- (m) *Loss of business or employment or both;*
- (n) *Any other claim arising out of or connected with, any activity of handling of hazardous substance.*

### **Tribunal to have Appellate Jurisdiction**

Section 16 provides that any person aggrieved by,—

- (a) an order or decision, made, on or after the commencement of the National Green Tribunal Act, 2010, by the appellate authority under section 28 of the Water(Prevention and Control of Pollution) Act, 1974;
- (b) an order passed, on or after the commencement of the National Green Tribunal Act, 2010, by the State Government under section 29 of the Water (Prevention and Control of Pollution) Act, 1974;
- (c) directions issued, on or after the commencement of the National Green Tribunal Act, 2010, by a Board, under section 33A of the Water (Prevention and Control of Pollution) Act, 1974;
- (d) an order or decision made, on or after the commencement of the National Green Tribunal Act, 2010, by the appellate authority under section 13 of the Water (Prevention and Control of Pollution) Cess Act, 1977;
- (e) an order or decision made, on or after the commencement of the National Green Tribunal Act, 2010, by the State Government or other authority under section 2 of the Forest (Conservation) Act, 1980;
- (f) an order or decision, made, on or after the commencement of the National Green Tribunal Act, 2010, by the Appellate Authority under section 31 of the Air(Prevention and Control of Pollution) Act, 1981;
- (g) any direction issued, on or after the commencement of the National Green Tribunal Act, 2010, under section 5 of the Environment (Protection) Act, 1986;
- (h) an order made, on or after the commencement of the National Green Tribunal Act, 2010, granting environmental clearance in the area in which any industries, operations or processes or class of industries, operations and processes shall not be carried out or shall be carried out subject to certain safeguards under the Environment (Protection) Act, 1986;
- (i) an order made, on or after the commencement of the National Green Tribunal Act, 2010, refusing to grant environmental clearance for carrying out any activity or operation or process under the Environment (Protection) Act, 1986;
- (j) any determination of benefit sharing or order made, on or after the commencement of the National Green Tribunal Act, 2010, by the National Biodiversity Authority or a State Biodiversity Board under the provisions of the Biological Diversity Act, 2002,

may, within a period of thirty days from the date on which the order or decision or direction or determination is communicated to him, prefer an appeal to the Tribunal. However, the Tribunal may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

### **Liability to pay relief or compensation**

Section 17 provides that where death of, or injury to, any person (other than a workman) or damage to any property or environment has resulted from an accident or the adverse impact of an activity or operation or process, under any enactment specified in Schedule I, the person responsible shall be liable to pay such relief or compensation for such death, injury or damage, under all or any of the heads specified in Schedule II, as may be determined by the Tribunal.

If the death, injury or damage caused by an accident or the adverse impact of an activity or operation or process under any enactment specified in Schedule I cannot be attributed to any single activity or operation or process but is the combined or resultant effect of several such activities, operations and processes, the Tribunal may, apportion the liability for relief or compensation amongst those responsible for such activities, operations and processes on an equitable basis. The Tribunal shall, in case of an accident, apply the principle of no fault.

### **Application or Appeal to the Tribunal**

Section 18 states that without prejudice to the provisions contained in section 16, an application for grant of relief or compensation or settlement of dispute may be made to the Tribunal by—

- (a) the person, who has sustained the injury; or
- (b) the owner of the property to which the damage has been caused; or
- (c) where death has resulted from the environmental damage, by all or any of the legal representatives of the deceased; or
- (d) any agent duly authorised by such person or owner of such property or all or any of the legal representatives of the deceased, as the case may be; or
- (e) any person aggrieved, including any representative body or organisation; or
- (f) the Central Government or a State Government or a Union territory Administration or the Central Pollution Control Board or a State Pollution Control Board or a Pollution Control Committee or a local authority, or any environmental authority constituted or established under the Environment (Protection) Act, 1986 or any other law for the time being in force;

However, where all the legal representatives of the deceased have not joined in any such application for compensation or relief or settlement of dispute, the application shall be made on behalf of, or, for the benefit of all the legal representatives of the deceased and the legal representatives who have not so joined shall be impleaded as respondents to the application. It has been classified that the person, the owner, the legal representative, agent, representative body or organisation shall not be entitled to make an application for grant of relief or compensation or settlement of dispute if such person, the owner, the Legal representative, agent, representative body or organization have preferred an appeal under section 16.

Sub section (3) prescribes that the application, or as the case may be, the appeal filed before the Tribunal shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the application, or, as the case may be, the appeal, finally within six months from the date of filing of the application, or as the case may be, the appeal, after providing the parties concerned an opportunity to be heard.

### **Procedure and Powers of Tribunal**

Sub-section (1) of Section 19 prescribes that, the Tribunal shall not be bound by the procedure laid down in the Code of Civil Procedure, 1908 but shall be guided by the principles of natural justice. The Tribunal has been empowered to regulate its own procedure and also not bound by the rules of evidence contained in the Indian Evidence Act, 1872.

Under Sub-section (4), the Tribunal, for the purpose of discharging its functions, has been entrusted with 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 namely:

- (a) summoning and enforcing the attendance of any person and examining him on oath;
- (b) requiring the discovery and production of documents;
- (c) receiving evidence on affidavits;
- (d) subject to the provisions of section 123 and 124 of the Indian Evidence Act, 1872, requisitioning any public record or document or copy of such record or document from any office;
- (e) issuing summons for the examination of witnesses or documents;
- (f) reviewing its decisions;
- (g) dismissing a representation for default or deciding it *ex parte*;
- (h) setting aside any order or dismissal of any representation for default or any order passed by it *ex parte*; and
- (i) pass an interim order (including granting an injunction or stay) after providing the parties concerned an opportunity to be heard, on any application made or appeal filed under this Act;
- (j) pass an order requiring any person to cease and desist from committing or causing any violation of any enactment specified in Schedule I;
- (k) any other matter which is required to be, or may be prescribed by the Central Government.

Sub section (5) provides that all proceedings before the Tribunal shall be deemed to be the judicial proceedings within the meaning of sections 193,219 and 228 for the purposes of section 196 of the Indian Penal Code and the Tribunal shall be deemed to be a civil court for the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

### **Tribunal to Apply Certain Principle**



*Section 20 provides that the Tribunal shall, while passing any order or decision or award, apply the principles of*

- *sustainable development,*
- *the precautionary principle and*
- *the polluter pays principle.*

### **Appeal to the Supreme Court**

Section 22 states that any person aggrieved by any award, decision or order of the Tribunal, may, file an appeal to the Supreme Court, within ninety days from the date of communication of the award, decision or order of the Tribunal, to him, on any one or more of the grounds specified in section 100 of the Code of Civil Procedure, 1908. However, the Supreme Court may entertain any appeal after the expiry of ninety days, if it is satisfied that the appellant was prevented by sufficient cause from preferring the appeal.

### **PENALTY**

#### **Penalty for failure to comply with order of the Tribunal**

Section 26 provides that whoever, fails to comply with any order or award or decision of the Tribunal, shall be punishable with imprisonment for a term which may extend to three years, or with fine which may extend to

ten crore rupees, or with both and in case the failure or contravention continues, with additional fine which may extend to twenty-five thousand rupees for every day during which such failure or contravention continues after conviction for the first such failure or contravention.

In case a company fails to comply with any order or award or a decision of the Tribunal, such company shall be punishable with fine which may extend to twenty-five crore rupees, and in case the failure or contravention continues, with additional fine which may extend to one lakh rupees for every day during which such failure or contravention continues after conviction for the first such failure or contravention.

Notwithstanding anything contained in the Code of Criminal Procedure, 1973, every offence under this Act shall be deemed to be non-cognizable within the meaning of the said Code.

### Offence by Companies

Section 27 deals with Offence by Companies and provides that where any offence has been committed by a company, every person who, at the time the offence was committed, was directly in charge of, and was responsible to the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. However, no person liable to any punishment, if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence. Where an offence has been committed by the company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Explanation to Section 27 classifies that—

- (a) "Company" means any body corporate and includes a firm or other association of individuals; and
- (b) "Director" in relation to a firm means a partner in the firm.

### Offence by Government Department

Section 28 provides that where any Department of the Government fails to comply with any order or award or decision of the Tribunal, the Head of the Department shall be deemed to be guilty of such failure and shall be liable to be proceeded against for having committed an offence and punished accordingly. However, such Head of the Department shall not be liable to any punishment if he proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence.

Where an offence has been committed by a Department of the Government and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of any officer, other than the Head of the Department, such officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

### LESSON ROUND UP

- National Green Tribunal has been constituted for the effective and expeditious disposal of cases relating to environmental protection and conservation of forests and other natural resources including enforcement of any legal right relating to environment and giving relief and compensation for damages to persons and property and for matters connected therewith or incidental thereto.
- "handling", in relation to any hazardous substance, means the manufacture, processing, treatment, package, storage, transportation, use, collection, destruction, conversion, offering for sale, transfer or the like of such hazardous substance

- "substantial question relating to environment" includes an instance where,—
  - (i) there is a direct violation of a specific statutory environmental obligation by a person by which,—
    - (A) the community at large other than an individual or group of individuals is affected or likely to be affected by the environmental consequences; or
    - (B) the gravity of damage to the environment or property is substantial; or
    - (C) the damage to public health is broadly measurable;
  - (ii) the environmental consequences relate to a specific activity or a point source of pollution.
- Tribunal consists of a full time Chairperson; and not less than ten but subject to maximum of twenty full time Judicial Members and not less than ten but subject to maximum of twenty full time Expert Members.
- The Chairperson of the Tribunal may, if considered necessary, invite any one or more persons having specialised knowledge and experience in a particular case before the Tribunal to assist the Tribunal in that case.
- Any person aggrieved by any award, decision or order of the Tribunal, may, file an appeal to the Supreme Court, within ninety days from the date of communication of the award, decision or order of the Tribunal, to him.
- The Supreme Court may entertain any appeal after the expiry of ninety days, if it is satisfied that the appellant was prevented by sufficient cause from preferring the appeal.
- Whoever, fails to comply with any order or award or decision of the Tribunal, shall be punishable with imprisonment for a term which may extend to three years, or with fine which may extend to ten crore rupees, or with both.
- In case a company fails to comply with any order or award or a decision of the Tribunal, such company shall be punishable with fine which may extend to twenty-five crore rupees.
- Every offence under this Act shall be deemed to be non-cognizable within the meaning of the Cr.PC.

### **SELF TEST QUESTIONS**

1. List out the Acts specified in the 1<sup>st</sup> Schedule to the National Green Tribunal Act?
2. Enumerate the powers and functions of National Green Tribunal?
3. Write short notes on sustainable development.
4. Explain precautionary principle in Pollution Laws.
5. List out the heads under which compensation or relief for damaged may be claimed under the National Green Tribunal Act.

# PREVENTION AND CONTROL OF AIR POLLUTION

## Section IV

### LESSON OUTLINE

- Preamble of the Air (Prevention and Control of Pollution) Act, 1981
- Air Pollution
- Air Pollutant
- Control Equipment
- Approved Appliances
- Central and State Pollution Control Boards
- Power and Function of the Central and State Board
- Composition of State Board
- Prevention and Control of Air pollution
- Restriction and use of Certain Industrial Plants
- State Air Laboratory
- Noise Pollution
- Offences and Penalty
- Power to Entry and Inspection
- Power to take samples
- Penalty and procedure

### **LEARNING OBJECTIVES**

The United Nations Conference on the Human Environment met at Stockholm from 5 to 16 June 1972, considered the need for a common outlook and for common principles to inspire and guide the peoples of the world in the preservation and enhancement of the human environment, Proclaims that the protection and improvement of the human environment is a major issue which affects the well-being of peoples and economic development throughout the world; it is the urgent desire of the peoples of the whole world and the duty of all Governments.

The air pollution and the resultant air quality can be attributed to emissions from transportation, industrial and domestic activities. The air quality has been, therefore, an issue of social concern in the backdrop of various developmental activities. The norms for ambient air quality and various industry specific emissions standards are notified from time to time by Government. For control of air pollution, Parliament enacted Air (Prevention and Control of Pollution) Act, 1981.

This section deals with air pollution, control equipment of any industrial plant, Air Pollution Control Area, restriction and use of certain industrial plant.

Air (Prevention and Control of Pollution) Act, 1981 an Act to provide the prevention, control and abatement of air pollution, for the establishment, with a view to carrying out the aforesaid purposes, of Boards, for conferring on and assigning to such Boards powers and functions relating thereto and for matters connected therewith.

## INTRODUCTION

Until the enactment of the Air (Prevention and Control of Pollution) Act, 1981, there was no concerted effort to legally control air pollution. No doubt, some of the States<sup>\*</sup> have had some enactments or the other to control the nuisance arising out of smoke and other emissions from factories but unfortunately the provisions of these enactments were not effectively enforced. Even the State Municipal Acts have not been effective in having sufficient control over air pollution. With a view to meeting the problem in more concrete terms, the Central Government initiated legislation to prevent pollution. The passing of Water (Prevention and Control of Pollution) Act, 1974 was the first step in this direction and subsequently in the year 1981 the Union Government decided to bring in another legislation to prevent air pollution exclusively. Thus came into being the Air (Prevention and Control of Pollution) Act, 1981. It is also necessary at this stage to note that India was one of the participants at the United Nations Conference on Human Environment held in Stockholm, in June 1972. Therefore, in order to give effect to the decisions taken at the conference, to take appropriate steps for the preservation of the natural resources of the earth which, among other things, included the preservation of the quality of air and control of air pollution, the Parliament enacted Air (Prevention and Control of Pollution) Act, 1981.

The Act came into force with effect from 16th day of May, 1981. It extends to the whole of India.

The Act, after it came into force, is being implemented by the Central and State Governments and the Central and State Boards. However, during the implementation of the Act, the implementing agencies experienced some administrative and practical difficulties in effectively implementing the provisions of the Act. The ways and means to remove these difficulties were examined by the Government in consultation with the various Central Government Departments and taking into account the views expressed the Government brought about various amendments to the Act through the Air (Prevention and Control of Pollution) Amendment Act, 1987.

## DEFINITIONS

Section 2 of the Act contains definitions of the terms used in the Act. The definitions of important terms such as Accident, Hazardous Substance, Handling, and the owner, are given below:

### **Air Pollutant [Section 2(a)]**

Air Pollutant means any solid, liquid or gaseous substance including noise present in the atmosphere in such concentration as may be or tend to be injurious to human beings or other living creatures or plants or property or environment.

### **Air Pollution [Section 2(b)]**

Air Pollution means the presence in the atmosphere of any air pollutant.

### **Approved Appliance [Section 2(c)]**

Approved appliance means any equipment or gadget used for the burning of any combustible material or for generating or consuming any fume, gas or particulate matter and approved by the State Board for the purpose of this Act.

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\* First ever pollution control law in India was probably brought under the British Rule in 1912. The Bombay Smoke Nuisance Act, 1912 – to control smoke emissions.

**Approved Fuel [Section 2(d)]**

Approved Fuel means any fuel approved by the State Board for the purposes of this Act.

**Automobile [Section 2(e)]**

Automobile means any vehicle powered either by internal combustion engine or by any method of generating power to drive such vehicle by burning fuel.

**Chimney [Section 2(h)]**

Chimney includes any structure with an opening or outlet from or through which any air pollution may be emitted.

**Control Equipment [Section 2(i)]**

Control Equipment means any apparatus, device, equipment or system to control the quality and manner of emission of any air pollutant and includes any device used for securing the efficient operation of any industrial plant.

**Emission [Section 2(j)]**

Emission means any solid or liquid or gaseous substance coming out of any chimney duct or flue or any other outlet.

**Industrial Plant [Section 2(k)]**

Industrial Plant means any plant used for any industrial or trade purpose and emitting any air pollutant into the atmosphere.

**Occupier [Section 2(m)]**

Occupier in relation to any factory or premises, means the person who has control over the affairs of the factory or the premises and includes in relation to any substance, the person in possession of the substance.

**State Board [Section 2(o)]**

State Board means,(i) in relation to a State in which the Water (Prevention and Control of Pollution) Act, 1974 is in force and the State Government has constituted for that State, a State Pollution Control Board under Section 4 of the Act, the said State Board; and (ii) in relation to any other State, the State Board for the Prevention and Control of Air Pollution constituted by the State Government under Section 5 of this Act.

**Central and State Pollution Control Boards**

Section 3 of the Act provides for the constitution of the Central Pollution Control Board for prevention and control of air pollution. Accordingly, the Central Pollution Control Board constituted under Section 3 of the Water (Prevention and Control of Pollution) Act, 1974 shall exercise the powers and perform the functions of the Central Pollution Control Board for the prevention and Control of Air Pollution under the Act.

Section 4 of the Act clarifies that at the State level in which the Water (Prevention and Control of Pollution) Act, 1974 is in force, and the State Government concerned has constituted a State Pollution Control Board then such State Board shall be the State Board for Prevention and Control of Air Pollution under the Act.

Section 5 of the Act provides that where, in any State there is no such State Pollution Control Board the State Government shall constitute a State Board for prevention and control of air pollution.

### **Composition of State Boards**

The State Board so constituted shall have the following members:

- (a) a Chairman, being a person having special knowledge or practical experience in respect of matters relating to environmental protection to be nominated by the State Government; provided that the Chairman may be either whole-time or part-time, as the State Government may think fit.
- (b) such number of officials, not exceeding five, as the State Government may think fit, to be nominated by the State Government to represent that Government.
- (c) such number of persons, not exceeding five, as the State Government may think fit, to be nominated by the State Government from amongst the members of the local authorities functioning within the State.
- (d) such number of non-officials, not exceeding three, as the State Government may think fit, to be nominated by the State Government to represent the interests of agriculture, fishery or industry or trade or labour or any other interest, which, in the opinion of the Government, ought to be represented.
- (e) two persons to represent the companies or corporations owned, controlled or managed by the State Government, to be nominated by that Government.
- (f) a full-time member-secretary having such qualifications, knowledge and experience of scientific, engineering or management aspects of pollution control as may be prescribed to be appointed by the State Government. The State Government should however ensure that not less than two of the members are persons having special knowledge or practical experience in respect of matters relating to the improvement of the quality of air or the prevention, control or abatement of air pollution.

Every State Board constituted under the Act shall be a body corporate with a name specified by the State Government, having perpetual succession and a common seal, with power, subject to the provisions of the Act, to acquire and dispose the property and to contract, and may, by the said name sue or be sued.

Section 6 of the Act provides that the Central Board shall exercise the powers and perform the functions of a State Board in any Union Territory. However the Central Board may delegate all or any of its powers and functions to any person or body of persons as the Central Government may specify.

Section 7 of the Act deals with terms and conditions of service of the members. A member of a State Board shall hold office for three years. Notwithstanding the expiration of his term, a member can hold office until his successor enters upon his office. The term of office of a member nominated by the State Government would come to an end as soon as he ceases to hold office under the State Government or as the case may be, the company, or corporation owned, controlled or managed by the State Government by virtue of which he was nominated. A member (other than a member secretary) may at any time resign, his office by writing under his hand to the Chairman. Likewise the Chairman can resign by writing to the State Government. Absence of a member from three consecutive meetings without sufficient reason would be deemed to be vacation of the office of the member.

A State Board has also been empowered to appoint a qualified person to be the consultant to the Board. A State Board may also, by general or special order, delegate to the Chairman or the member secretary or any officer of the Board such powers and functions as it may deem necessary (Section 15).

Section 8 of the Act deals with disqualification for a person to be a member of a State Board. Accordingly, no person can be a member of the State Board constituted under the Act, who

- (a) is or at any time has been, adjudged insolvent, or
- (b) is of unsound mind and has been so declared by a competent court, or
- (c) is, or has been, convicted of an offence which, in the opinion of the State Government, involves moral turpitude, or
- (d) is, or at any time, has been, convicted of an offence under this Act, or
- (e) has directly or indirectly, by himself or by any partner, any share or interest in any firm or company carrying on the business of manufacture, sale or hire of machinery, industrial plant, control equipment or any other apparatus for the improvement of quality of air or for the prevention, control or abatement of air pollution, or
- (f) is a director or a secretary, manager or other salaried officer or employee of any company or firm having any contract with the Board or with the Government constituting the Board or with a local authority in the State, or with a company or corporation owned, controlled or managed by the Government for the carrying out of programmes for the improvement of the quality of air or for the prevention, control, or abatement of air pollution, or
- (g) has so abused, in the opinion of the State Government, his position as a member, as to render his continuance on the State Board detrimental to the interest of the general public.

The State Government is empowered by order in writing, remove any member who is or has become, subject to any disqualification mentioned above after giving a reasonable opportunity to the member concerned to show cause against such removal.

Under Section 9 of the Act if a member of State Board becomes subject to any of the disqualifications mentioned in the Section 8, his seat shall become vacant. Section 10 of the Act deals with meetings of the Board. Accordingly, the Board shall meet at least once in three months and shall observe the rules of procedure prescribed therefor. The Chairman of the Board, however, has powers to convene meeting at such times as he thinks fit, for transacting any business of urgent nature. Copies of the minutes of the meeting are required to be forwarded to the Central Board and to the State Government concerned.

Section 11 of the Act empowers the constitutions of such number of committees of the Board as may be found necessary.

Section 12 of the Act entitles the Board to associate with itself in such manner and for such purpose as may be prescribed, any person whose assistance or advice it may desire to obtain in performing any of its functions under the Act. Such a person, however, shall not have a right to vote at the meeting of the Board. He can, however, participate in the discussions of the Board, relevant to the purpose for which he was associated with the Board.

### **Powers and Functions of the Central Board**

Chapter III of the Act deals with powers and functions of the Board. In terms of Section 16, the main functions of the Central Board are to improve the quality of the air and to prevent, control or abate air pollution in the country. In particular and without prejudice to the generality of the above functions, the Central Board may:

- (a) advise the Central Government on any matter concerning the improvement of the quality of air and prevention, control or abatement of air pollution;

- (b) plan and cause to be executed a nation-wide programme for the prevention, control or abatement of air pollution;
- (c) co-ordinate the activities of the State Boards and resolve disputes among them;
- (d) provide technical assistance and guidance to the State Boards, carry out and sponsor investigations and research relating to problems of air pollution and prevention, control or abatement of air pollution.
- (dd) perform such of the function of any State Board as may be specified in an order made under Sub-section (2) of Section 18.
- (e) plan and organize the training of persons engaged or to be engaged in programmes for the prevention, control and abatement of air pollution on such terms and conditions as the Central Board may specify;
- (f) organise through mass media, a comprehensive programme regarding the prevention, control or abatement of air pollution;
- (g) collect, compile and publish technical and statistical data relating to air pollution and the measures devised for its effective prevention, control and abatement and prepare manuals, codes or guides relating to prevention, control or abatement of air pollution;
- (h) lay down standards for the quality of air;
- (i) collect and disseminate information in respect of matters relating to air pollution;
- (j) perform such other functions as may be prescribed.

The Central Board has been empowered to establish or recognise a laboratory or laboratories to enable the Central Board to perform its functions efficiently. It also has powers to delegate any of its functions generally or specially to any of the committees appointed by it.

### **Functions of the State Board**

Section 17 of the Act dealing with functions of the State Boards, enumerates the following functions of the State Boards:

- (a) to plan a comprehensive programme for the prevention, control or abatement of air pollution and to secure the execution thereof;
- (b) to advise the State Government on any matter concerning the prevention, control or abatement of air pollution;
- (c) to collect and disseminate information relating to air pollution;
- (d) to collaborate with the Central Board in organising the training of the persons engaged or to be engaged in programmes relating to prevention, control or abatement of air pollution and to organise mass-education programme relating thereto;
- (e) to inspect, at all reasonable times, any control equipment, industrial plant or manufacturing process and to give, by order, such directions to such persons as it may consider necessary to take steps for the prevention, control or abatement of air pollution;
- (f) to inspect air pollution control areas at such intervals as it may think necessary, assess the quality of air pollution and take steps for the prevention, control or abatement of pollution in such areas;
- (g) to lay down, in consultation with the Central Board and having regard to the standards for the quality of air laid down by the Central Board, standards for emission of air pollutants into the atmosphere

from industrial plants and automobiles or for the discharge of any air pollutant into the atmosphere from any other source whatsoever not being a ship or an aircraft;

Provided that different standards for emission may be laid down under this clause for different plants having regards to the quantity and composition of emission of air pollutants into the atmosphere from such industrial plants.

- (h) to advise the State Government with respect to the suitability of any premises or location for carrying on any industry which is likely to cause air pollution;
- (i) to perform such other functions as may be prescribed or as may, from time to time, be entrusted to it by the Central Government or the State Government;
- (j) to do such other things and to perform such other acts as it may think necessary for the proper discharge of its functions and generally for the purpose of carrying into effect the purposes of this Act.

In terms of Section 18 of the Act, the Central Board shall be bound by the directions given to it in writing by the Central Government. Similarly, State Boards shall be bound by the directions given to them by Central Board or the State Government.

Where the direction given by the State Government is inconsistent with the direction given by the Central Government, the matter shall be referred to the Central Government for its decision. Where the Central Government is of the opinion that any State Board has defaulted in complying with any directions given by the Central Board and as a result of such default a grave emergency has arisen and it is expedient, in public interest so to do, it may direct the Central Board to perform any of the functions of the State Board in relation to such area as may be specified in the order.

### **Prevention and Control of Air Pollution**

Chapter IV of the Act contains detailed provisions for prevention and control of air pollution. Section 19 empowers the State Government to declare, after consultation with the State Board, any area or areas within the State as air pollution control area or areas for the purpose of the Act. The State Government has been authorised to alter any air pollution control area by way of extension or reduction and also declare a new air pollution control area by merging one or more existing air pollution control area or areas or any part or parts thereof.

If the State Government after consultation with the State Board is of the opinion that the use of any fuel other than approved fuel, in any air pollution control area or part thereof, may cause or is likely to cause air pollution, it may, by notification in the Official Gazette, prohibit the use of such fuel in such area or part thereof with effect from such date (being not less than three months from the date of publication of the notification) as may be specified in the notification.

The Government may, after consultation with the State Board, by notification in the Official Gazette, direct that with effect from such date as may be specified therein, no appliance, other than an approved appliance, shall be used in the premises situated in an air pollution control area. However different dates may be specified for different parts of an air pollution control area or for the use of different appliances.

If the State Government, after consultation with the State Board, is of the opinion that burning of any material (not being fuel) in any air pollution control area or part thereof may cause or is likely to cause air pollution, it may, by notification in the Official Gazette, prohibit the burning of such material in such area or part thereof.

Under Section 20 of the Act, The State Government shall, in consultation with the State Board, give such instructions as it may deem necessary to the concerned authority incharge of registration of motor vehicles

under the Motor Vehicles Act, 1939 (now Motor Vehicles Act, 1988), with a view of ensuring that standards for emission of air pollutants from automobiles laid down by the State Board are complied with.

#### **Air Pollution Control Area – Powers of State**



*In Orissa State Prevention and Control of Pollution Board vs. Orient Paper Mills and another (AIR 2003 SC 1966). Supreme Court observed that even if the State Government has not framed rules prescribing the manner in which the area is to be declared as air pollution control area, the State Government is empowered to declare any area within the State as an Air Pollution Control Area by notification in the Official Gazette. It may, however, be after consultation with Board and in the manner as may be prescribed. Absence of Rules will not render the Act inoperative. The Act under section 19 vests the State Government with power to notify any area, in an official gazette, as Air Pollution Control Area, but it can not be said that the exercise of such power is solely dependent upon framing of the rules prescribing the manner in which an area may be declared as Air Pollution Control Area.*

#### **Restrictions on Use of Certain Industrial Plants**

Section 21 of the Act deals with restriction on use of certain industrial plants. Accordingly, no person is allowed, without the previous consent of the State Board, to establish or operate any industrial plant in an air pollution control area. Prior to amendment in 1987 this section required only industries specified in the Schedule to the Act to obtain such consent. However, the amended section, with effect from 1st April, 1988 requires every industrial plant in an air pollution control area to obtain prior approval.

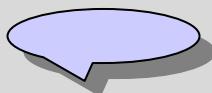
Application for approval of the State Board should be made in the prescribed Form alongwith the prescribed fee. The Rules framed by the respective State Governments specify the procedure for making such applications.

In case, a person operates in any such air pollution control area, from a date prior to the date of declaration of the area as an air pollution control area, such person is also required to make the application in the prescribed manner within 3 months of the declaration of that area to be an air pollution control area. In that case, he shall be deemed to be operating such industrial plants with the consent of the State Board.

Within a period of four months after the receipt of the application, the State Board should, by order in writing and reasons to be recorded in the order, grant the consent applied for, subject to such conditions and for such period as may be specified therein or refuse such consent.

It shall however be open to the State Board to cancel such consent before the expiry of the period for which it was granted or refuse further consent after such expiry if the conditions subject to which such consent was granted have not been fulfilled. But before cancelling the consent or refusing a further consent a reasonable opportunity of being heard should be afforded to the concerned person.

***Every person to whom consent has been granted by the State Board has been put under obligation to comply with the following conditions stipulated under Section 21(5), namely:***



- (i) *the control equipment of such specification as the State Board may approve in this behalf shall be installed and operated in the premises where the industry is carried on or proposed to be carried on;*

- (ii) the existing control equipment, if any, shall be altered or replaced in accordance with the directions of the State Board;
- (iii) the control equipment referred to in clause (i) or clause (ii) shall be kept at all times in good running condition;
- (iv) chimney, wherever necessary, of such specifications as the State Board may approve in this behalf shall be erected or re-erected in such premises;
- (v) such other conditions as the State Board may specify in this behalf, and
- (vi) the conditions referred to in clause (i), (ii) and (iv) shall be complied with within such period as the State Board may specify in this behalf. In the case of a person operating any industrial plant in an air pollution control area immediately before the date of declaration of such area as an air pollution control area, the period so specified shall not be less than six months. Further, after the installation of any control equipment or after the alteration or replacement of any control equipment or after the erection or re-erection of any chimney, no control equipment or chimney shall be altered, or replaced or, as the case may be, erected or re-erected except with the previous approval of the State Board.

The State Board has been empowered to vary all or any of the conditions if due to technology improvement or otherwise, it is of the opinion that all or any of those conditions require(s) any variation including change of any control equipment either in whole or in part.

Where a person to whom consent has been granted by the State Board to operate an industrial plant transfers his interest in the industry to any other person, then the consent given by the State Board shall be deemed to have been granted to such other persons who shall be bound to comply with all the conditions subject to which such consent was originally granted.

Emission of air pollution in excess of the standards laid down by the Board is prohibited under Section 22. Accordingly no person operating any industrial plant in any air pollution control area is allowed to discharge or cause or permitted to be discharged the emission of any air pollution in excess of the standards laid down by the State Board under Section 17(1)(g).

Section 22A inserted by the 1987 Amendment Act empowers the Board to make application to court for restraining persons from causing air pollution. Where it is apprehended by the Board that emission of any air pollutant in excess of the standards laid down is likely to occur by reason of any person operating an industrial plant or otherwise in any air pollution control area, it may make an application to a Court not inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of the First Class for restraining such person from emitting such air pollutant. On receipt of the application the Court may make such order as it may deem fit. Where the Court makes an order restraining any person from discharging or causing or permitting to be discharged the emission of any air pollutant it may direct such person to desist from taking such action as is likely to cause emission. If such direction is not complied with then the Court may authorise the Board to implement the direction in such manner as may be specified by the Court. All expenses incurred by the board in implementing the directions of the Court, are recoverable from the person concerned as arrears of land revenue or of public demand.

#### **Furnishing of Information to State Board and other Agencies in Certain Cases**

Section 23 of the Act imposes an obligation on the person in charge of the premises where emission of any air pollutant occurs or is apprehended, to furnish the fact of any occurrence or apprehension of emission of

any air pollutant into the atmosphere in excess of the standards laid down by the State Board. Even where the person in charge of the premises apprehends that any air pollutant in excess of these standards is likely to occur due to any accident or other unforeseen act or event, he has to intimate such apprehension to the State Board and to such authorities or agencies as may be prescribed. The State Board or any authority or agency, as the case may be, shall, on receipt of such information, cause such remedial measures to be taken as are necessary to mitigate the emission of such air pollutants. Expenses if any, incurred by the State Board, authority or agency as the case may be, with respect to any such remedial measure shall be recovered from the person in charge of the premises as if they are arrears of land revenue or of public demand.

### **Power to Entry and Inspection**

Under Section 24 of the Act, the State Board is empowered to authorise any person to enter into any place, with such assistance as he considers necessary, for the purpose of:

- (a) performing any of the functions of the State Board;
- (b) determining whether and if so in what manner, any such functions are to be performed or whether any provisions of the Act or Rules made thereunder or any notice, order, direction or authorisation served, made, given or granted under the Act is being or has been complied with;
- (c) examining and testing any control equipment, industrial plant, record, register, document or any material object or for conducting a search of any place in which he has reason to believe that an offence under this Act or the Rules made thereunder has been or is being or is about to be committed and for seizing any such control equipment, industrial plant, record, register, document or other material object, he has reason to believe that it may furnish evidence of the commission of an offence punishable under this Act or the Rules made thereunder.

Every person is bound to render all assistance to the person empowered by the State Board to enter such premises for inspection. A person who wilfully delays or obstructs entry of such person into the premises shall be guilty of an offence under the Act. The provisions of the Code of Criminal Procedure 1973 or any other similar code where the Cr. P.C. is not in force, shall apply so far as may be to any search or seizure, as they apply to any search or seizure under the authority of a warrant issued under Section 94 of the Cr. C.P. or as the case may be, under the corresponding provision of the State law.

### **Power to Obtain Information**

For the purposes of carrying out the functions entrusted, the State Board or any officer empowered may call for any information including information regarding the types of air pollutants emitted into the atmosphere and the level of the emission of such air pollutants, from the occupier or any other person carrying on any industry or operating any control equipment or industrial plant. Also for the purposes of verifying the correctness of such information, the State Board or such officer shall have the right to inspect the premises where such industry, control equipment or industrial plant is being carried on or operated. After the 1987 amendments, this section has empowered the Board to obtain information from industries operating even outside the air pollution control areas.

### **Power to Take Samples**

Section 26 of the Act empowers the State Boards or any other officer empowered by it to take for the purpose of analysis, samples of air or emission from any chimney, flue or duct or any other outlet in such manner as may be prescribed.

The result of analysis of such samples shall not be admissible in evidence in any legal proceeding unless the following are compiled with:

- (1) When a sample of emission is taken, the person taking the sample shall
  - (a) serve on the occupier or his agent, a notice, then and there, in such form as may be prescribed, of his intention to have it so analysed;
  - (b) in the presence of the occupier or his agent collect a sample of emission for his analysis;
  - (c) cause the sample to be placed in a container or containers to be marked, sealed and signed by both the persons taking the sample and the occupier or his agent;
  - (d) send, without delay, the container to the laboratory established or recognised by the State Board or to any State Air Laboratory specified under Section 28 of the Act, and
- (2) When a sample of emission is taken and the person taking the sample serves the notice as specified above then
  - (a) in case the occupier or his agent wilfully absents himself, the person taking the sample shall collect the sample of emission for analysis to be placed in a container or containers which shall be marked, sealed and signed by the person taking the sample, and
  - (b) in case the occupier or his agent is present at the time of taking the sample but refuses to sign the marked and sealed container or containers of the sample of emission, the marked and sealed container or containers shall be signed by the person taking the sample and sent to the laboratory for analysis.

### **Report of Analysis**

Where the sample of emission has been sent to the laboratory, the same shall be analysed and the report thereof shall be submitted in the prescribed form in triplicate to the State Board. On receipt of the report, the State Board shall send one copy of the same to the occupier or his agent of the premises, wherefrom the samples were taken, the second copy shall be preserved for production before the Court in any legal proceedings and the other copy shall be kept by the State Board. Any cost incurred in conducting such analysis shall be borne by the occupier of the premises from where the samples were taken as if they are arrears of land revenue or of public demand.

### **State Air Laboratory**

The State Government have been authorised to establish, by notification in the Official Gazette, one or more laboratories or specify one or more laboratories to carry out functions entrusted to the State Air Laboratory under the Act. The State Government may after consultation with the State Board, make rules prescribing the functions of the State Air Laboratory, the procedure for submission to the State Laboratory of samples for analysis and reports thereon and the fees payable in respect of such reports and such other matter as may be necessary or expedient to enable that Laboratory to carry out its functions.

Section 29 of the Act empowers the State Government to appoint such persons as it thinks fit having the prescribed qualifications, as Government analysts for the purpose of analysis of samples of air or emissions.

### **Appeal**

Section 31 of the Act dealing with appeal provides that any person aggrieved by an order of the State Board may within 30 days from the date on which the order is communicated to him, prefer an appeal to such authority as the State Government may think fit to constitute. The appellate authority may entertain appeals beyond the 30 days period if such authority is satisfied that the appellant was prevented by sufficient cause

from filing the appeal in time. The appellate authority is bound to dispose of the appeal as expeditiously as possible after giving the appellant and the State Board a reasonable opportunity of being heard.

### **Power to Give Directions**



*Section 31A inserted by the Air (Prevention and Control of Pollution) Amendment Act, 1987 empowers the Board to give certain directions. This is a very important provision in view of the nature of the directions that could be given thereunder. This section has been given overriding effect upon other laws. This section provides that notwithstanding anything contained in any other law but subject to the provisions of the Air (Prevention and Control of Pollution) Act and any directions, that may be given by the Central Government, the Board may issue any directions in writing to any person, officer or authority, and such person, officer or authority shall be bound to comply with such directions. The power to issue direction would include the power to direct (i) closure; prohibition or regulation of any industry, operation and process; or (ii) the stoppage, or regulation of supply of electricity, water or any other service.*

### **Penalties and Procedure**

Chapter VI of the Act contains provisions relating to penalties and other procedures. Under Section 37, failure to comply with the provisions of Section 21 (consent for establishment or operation of industrial plant in an air pollution control area); or Section 22 (emission of air pollutant in excess of the prescribed standards) or directions issued under Section 31A (closure, prohibition, regulation, stoppage of electricity, water etc.), are punishable with imprisonment for a term which shall not be less than one year and six months but which may extend to six years and with fine. Where failure continues, an additional fine is also leviable which may extend to ₹5,000 for every day of continuing failure after the conviction for the first such failure. Where the above failure continues beyond a period of one year after the date of conviction, the offender shall be punishable with imprisonment for a term which shall not be less than two years but which may extend to seven years and with fine.

Under Section 38 whoever does following acts shall be punishable with imprisonment for a term which may extend to three months or with fine which may extend to ₹10,000 or with both:

- (a) destroys, pulls down, removes, injures, or defaces any pillars post or stake fixed in the ground or any notice or other matter put up, inscribed, or placed by or under the authority of the Board; or
- (b) obstructs any person acting under the orders or directions of the Board from exercising his powers and performing his functions under the Act; or
- (c) damages any works or property belonging to the Board; or
- (d) fails to furnish to the Board or any officer or employee of the Board any information required by the Board or such officer or employee for the purposes of the Act; or
- (e) fails to intimate the occurrence of the emission of air pollutants into the atmosphere in excess of the standards laid down by the State Board or the apprehension of such occurrence, to the State Board and other prescribed authorities or agencies as required by Section 23(1); or
- (f) in giving any information which he is required to give under the Act, makes a statement which is false in any material particular; or
- (g) for the purposes of obtaining any consent under Section 21 makes a statement which is false in any material particular.

In terms of Section 39, the contravention of any provisions of the Act or any order or direction issued thereunder for which no penalty has been provided in the Act, has been made punishable with imprisonment for a term which may extend to three months or with fine which may extend to ₹10,000 or both. Continuing contravention would attract an additional fine of ₹ 5000 for everyday during which the contravention continues.

Section 40 specifically deals with offences by companies. Accordingly, where an offence has been committed under the Act by a company, every person who, at the time of commission of such offence was directly in charge of and responsible to the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. Where, however, any person proves that the offence was committed without his knowledge or that he exercised due diligence to prevent commission of such offence, nothing shall render him liable for any punishment. This section further provides for punishment to any person who consents or connives at any offence or where the offence is attributable to the neglect on the part of any director, manager, secretary or other officer of the company.

### **Cognizance of Offences**

Section 43 provides that no Court shall take cognizance of any offence under the Act except on a complaint made by (a) a Board or any officer authorised in that behalf, or (b) any person who has given notice of not less than sixty days in prescribed manner, of the alleged offence and of his intention to make a complaint to the Board or an officer authorised. No Court inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of the first class shall try any offence punishable under the Act. Where any person makes a complaint as above, the Board shall, on demand, make available the relevant reports to that person. The Board can refuse to make available such reports, if it is against public interest.

### **State Government to Supersede State Board**

Section 47 of the Act confers an important power on the State Government to supersede the State Board. The State Government, under this section, can supersede the State Board if it is of opinion that the Board has persistently made default in the performance of the functions imposed on it by or under the Act, or that circumstances exist which render it necessary in the public interest so to do; by notification in the Official Gazette for a period of not exceeding six months. Where the supersession has to be done on ground of default, a reasonable opportunity shall be given to the State Board concerned before the notification superseding the Board is issued. On issue of the supersession notification, the following consequence will follow:

- (a) all members of the Board shall vacate their offices as such;
- (b) all powers and functions as well as duties of the Board shall be performed or discharged by such person or persons as the State Government may direct;
- (c) all property owned or controlled by the State Board shall, until the Board is reconstituted, vest in the State Government.

On the expiry of the period of supersession, the State Government may extend the period of supersession for such time not exceeding six months or reconstitute the State Board by a fresh nomination, as the case may be. Even a person who has vacated the office by virtue of the supersession is eligible for nomination or appointment.

### Control of Noise Pollution



*In Bijayanada Patra and others vs. District Magistrate, Cuttack and Others (AIR 2000 Orissa 70, 71). Orissa High Court observed that noise pollution simply connotes unwanted sound in the atmosphere. It is unwanted because it lacks the agreeable musical quality. Noise is therefore, sound, but it is pollution when the effects of sound become undesirable. Noise not only causes irritation or annoyance but it does also constrict the arteries, and increase the flow of adrenaline and forces the heart to work faster, thereby accelerating the rate of cardiac ailments, the reason of being that continuous noise causes an increase in the cholesterol level resulting in rearmament constriction of blood vessels, making one prone to heart attacks and strokes. The health experts are of opinion that excessive noise can also lead to neurosis and nervous breakdown. Where noise can be said to amount to nuisance, the person causing noise can be restrained by injunctions even though that person was causing noise in the course of conduction his business.*

In order to control the noise pollution caused from various sources such as industrial activity, construction activity, generator sets, loud speakers, public address system, music systems, vehicular horns and other mechanical devices the Central Government has framed certain rules known as 'The Noise Pollution (Regulation and Control) Rules, 2000. The rules provide for the ambient air quality standard in respect of noise for different areas/zones. An area comprising 100 metres around hospitals, educational institutions and courts has been declared as the silence area/zone. The ambient air quality standards shall also be considered by the all development authorities, local bodies while taking any development activity. A loud speaker or a public address system shall not be used at night (between 10:00 p.m. to 6:00 a.m.) except in closed premises for communication. Whoever commits any offence of playing music or uses any sound amplifiers, beats a drum or blows a horn, etc. in a silence zone/area shall be liable to a penalty.

#### **What do you mean by noise pollution?**

*Noise pollution simply connotes unwanted sound in the atmosphere. It is unwanted because it lacks the agreeable musical quality. Noise is therefore, sound, but it is pollution when the effects of sound become undesirable*



### LESSON ROUND UP

- Air (Prevention and Control of Pollution) Act, 1981 to provide the prevention, control and abatement of air pollution, for the establishment, with a view to carrying out the aforesaid purposes, of Boards, for conferring on and assigning to such Boards powers and functions relating thereto and for matters connected therewith.
- Air Pollution means the presence in the atmosphere of any air pollutant.
- Air Pollutant means any solid, liquid or gaseous substance including noise present in the atmosphere in such concentration as may be or tend to be injurious to human beings or other living creatures or plants or property or environment.
- Control Equipment means any apparatus, device, equipment or system to control the quality and manner of emission of any air pollutant and includes any device used for securing the efficient operation of any industrial plant.

- Section 19 empowers the State Government to declare, after consultation with the State Board, any area or areas within the State as air pollution control area or areas for the purpose of the Act. The State Government has been authorised to alter any air pollution control area by way of extension or reduction and also declare a new air pollution control area by merging one or more existing air pollution control area or areas or any part or parts thereof.
- Section 21 of the Act deals with restriction on use of certain industrial plants. Accordingly, no person is allowed, without the previous consent of the State Board, to establish or operate any industrial plant in an air pollution control area.
- Emission of air pollution in excess of the standards laid down by the Board is prohibited under Section 22. Accordingly no person operating any industrial plant in any air pollution control area is allowed to discharge or cause or permitted to be discharged the emission of any air pollution in excess of the standards laid down by the State Board
- Board may issue any directions in writing to any person, officer or authority, and such person, officer or authority shall be bound to comply with such directions. The power to issue direction would include the power to direct (i) closure; prohibition or regulation of any industry, operation and process; or (ii) the stoppage, or regulation of supply of electricity, water or any other service.
- In order to control the noise pollution caused from various sources such as industrial activity, construction activity, generator sets, loud speakers, public address system, music systems, vehicular horns and other mechanical devices the Central Government has framed rules known as 'The Noise Pollution (Regulation and Control) Rules, 2000.

### SELF TEST QUESTIONS

1. Briefly explain the objective of Air (Prevention and Control of Pollution) Act, 1981.
2. Enumerate the powers and functions of State Pollution Control Board.
3. Write short notes on
  - (i) Air Pollution
  - (ii) State Air Laboratory
4. Explain Noise Pollution in Environment.
5. Enumerate briefly the restriction on use of Certain Industrial Plant.

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# PREVENTION AND CONTROL OF WATER POLLUTION

## Section V

### LESSON OUTLINE

- Objective of Water (Prevention and Control of Pollution) Amendment Act, 1988
- Meaning of water pollution
- Outlet
- Sewage effluent
- Stream
- Trade effluent
- Constitution of Central and State Pollution Control Board
- Functions of the Central and State Pollution Control Board
- Prevention and Control of Water Pollution
- Restriction New Outlets and New Discharges
- Emergency measure
- Power of the Board
- Appeal
- Offences and Penalty
- Offences by companies

### **LEARNING OBJECTIVES**

The United Nations Conference on the Human Environment which took place at Stockholm in 1972 proclaims that man has constantly to sum up experience and go on discovering, inventing, creating and advancing. In our time, man's capability to transform his surroundings, if used wisely, can bring to all peoples the benefits of development and the opportunity to enhance the quality of life. Wrongly or heedlessly applied, the same power can do incalculable harm to human beings and the human environment. We see around us growing evidence of man-made harm in many regions of the earth: dangerous levels of pollution in water, air, earth and living beings; major and undesirable disturbances to the ecological balance of the biosphere; destruction and depletion of irreplaceable resources; and gross deficiencies, harmful to the physical, mental and social health of man, in the man-made environment, particularly in the living and working environment.

India is a party to the decisions taken at the United Nations Conference on Human Environment held at Stockholm, in which India participated, calling upon the states to take appropriate steps for the Protection and Improvement of the human environment.

Parliament passed the Water (Prevention and Control of Pollution) Act, 1974 for prevention and control of water pollution. Therefore, it is essential for the students to be familiar with the law relating to prevention and control of water pollution and maintaining or restoring wholesomeness of water.

“Article 51-A of the Constitution imposes as one of the fundamental duties on every citizen, the duty to protect and improve the natural environment including forests, lakes, rivers and wildlife and to have compassion for living creatures.”

## OBJECTIVE OF THE ACT

*Water (Prevention and Control of Pollution) Act, 1974 has been enacted to provide for the prevention and control of water pollution and maintaining or restoring wholesomeness of water, for the establishment of Boards, with a view to carrying out these purposes, for the prevention and control of water pollution, for conferring on and assigning to such Boards powers and functions relating thereto and for matters connected therewith.*

In order to remove administrative and practical difficulties that emerged during the enforcement of the Act, many of the provisions were amended by the Water (Prevention and Control of Pollution) Amendment Act, 1988.

## DEFINITIONS

The definitions of certain terms used in the Act are important to understand the provisions of the Act. These are given below:

**Board** means the Central Board or a State Board. [Section 2(a)]

**Central Board** means the Central Pollution Control Board constituted under Section 3 [Section 2(b)]. Prior to the enactment of the 1988 Amendment Act Central Board meant the Central Board for Prevention and Control of Water Pollution. Since the Central Board deals with both Water and Air Pollution Control, it has been renamed as Central Pollution Control Board.

**Occupier** in relation to any factory or premises means the person who has control over the affairs of the factory or the premises and includes in relation to any substance, the person in possession of the substance [Section 2(d)].

**Outlet** includes any conduit pipe or channel, open or closed, carrying sewage or trade effluent or any other holding arrangement which causes, or is likely to cause, pollution. [Section 2(dd)]

**Pollution** means such contamination of water or such alteration of the physical, chemical or biological properties of water or such discharge of any sewage or trade effluent or any other liquid, gaseous or solid substance into water (whether directly or indirectly) as may, or is likely to, create a nuisance or render such water harmful or injurious to public health or safety, or to domestic, commercial, industrial, agricultural or other legitimate uses, or to the life and health of animals or plants or of aquatic organisms. [Section 2(e)]

**Sewage effluent** means effluent from any sewerage system or sewage disposal works and includes sullage from open drains. [Section 2(g)].

**Stream, the term stream includes:**

- (a) river;
- (b) water course (whether flowing or for the time being dry);
- (c) inland water (whether natural or artificial);
- (d) sub-terranean waters;
- (e) sea or tidal waters to such extent or, as the case may be, to such point as the State Government may, by notification in the Official Gazette, specify in this behalf. [Section 2(j)]

**Trade effluent** includes any liquid, gaseous or solid substance which is discharged from any premises used for carrying on any industry, operation or process or treatment and disposal system, other than domestic sewage. [Section 2(k)]

### Constitution of Central Pollution Control Board

Section 3 of the Act empowers the Central Government to constitute a Central Pollution Control Board to exercise such powers and functions as may be conferred upon it. The Central Board shall consist of the following members, namely:

- (a) a full-time Chairman, being a person having special knowledge or practical experience in respect of matters relating to environmental protection or a person having knowledge and experience in administering institutions dealing with the matters aforesaid, to be nominated by the Central Government;
- (b) such number of officials not exceeding five to be nominated by the Central Government to represent that Government.
- (c) such number of officials not exceeding five to be nominated by the Central Government from amongst the members of the State Boards, of whom not exceeding two shall be from amongst the members of the local authorities functioning within the state;
- (d) such number of non-officials not exceeding three to be nominated by the Central Government to represent the interests of agriculture, fishery or industry or trade or any other interest, which, in the opinion of the Central Government, ought to be represented;
- (e) two persons to represent the companies or corporations owned, controlled or managed by the Central Government, to be nominated by that Government;
- (f) a full time member secretary possessing qualifications and experience of scientific, engineering or management aspects of pollution control, to be appointed by the Central Government.

The Central Board shall be a body corporate with a perpetual succession and common seal with a right to own property and right to sue or to be sued.

### Constitution of State Pollution Control Board

Section 4 of the Act empowers the State Government to constitute the State Boards. The composition of a State Board shall be the following, namely:

- (a) a Chairman, being a person having special knowledge or practical experience in respect of matters relating to environmental protection or a person having knowledge and experience in administering institutions dealing with the matters aforesaid, to be nominated by the State Government. However, the Chairman may be either whole-time or part-time, as the State Government may think fit;
- (b) such number of officials not exceeding five, to be nominated by the State Government to represent that Government;
- (c) such number of persons not exceeding five to be nominated by the State Government from amongst the members of the local authorities functioning within the State;
- (d) such number of non-officials not exceeding three, to be nominated by the State Government to represent the interests of agriculture, fishery or industry or trade or labour or any other interests, which, in the opinion of the Government, ought to be represented;
- (e) two persons to represent the companies or corporations owned, controlled or managed by the State Government to be nominated by that Government;

- (f) a full-time member secretary having such qualifications, knowledge and experience of scientific, engineering or management aspects of pollution control to be appointed by the State Government.

The State Board shall also be a body corporate as is the Central Board.

The Central Board shall exercise the powers under the Act in relation to a Union Territory. The Central Board may however, delegate its powers in relation to any Union Territory to any person or body of persons.

Section 5 of the Act deals with terms and conditions of service of members. Briefly speaking a member other than a member secretary is entitled to hold office for three years. Notwithstanding the expiry of his term, a member may continue to hold office till his successor enters upon his office. The term of office of a member nominated by the Central/State Government shall come to an end as soon as he ceases to hold office under the Central/State Government etc. Any member of the board may be removed before the expiry of his term of office, after giving a reasonable opportunity of showing cause against such removal. The Chairman or member could resign the office by writing under his hand. A casual vacancy could be filled by a fresh nomination. A member is eligible for renomination. Other terms and conditions of service of the chairman and members shall be such as prescribed in the rules.

### **Disqualifications**

Section 6 of the Act deals with disqualification of a person to be a member of the Board. Accordingly, no person shall be a member of a Board, who:

- (a) is or at any time has been adjudged insolvent or has suspended payment of his debt or has compounded with his creditors, or
- (b) is of unsound mind or stands so declared by a competent court, or
- (c) is, or has been convicted of an offence which, in the opinion of the Central Government, or as the case may be, of the State Government, involves moral turpitude, or
- (d) is, or at any time, has been, convicted of an offence under this Act, or
- (e) has directly or indirectly, by himself or by any partner, any share or interest in any firm or company carrying on the business of manufacture, sale or hire of machinery, industrial plant, equipment, apparatus or fittings for the treatment of sewage or trade effluents, or
- (f) is a director or a secretary, manager or other salaried officer or employee of any company or firm having any contract with the Board, or with the Government constituting the Board, or with a local authority in the State, or with a company or corporation owned, controlled or managed by the Government, for the carrying out of sewage schemes or for the installation of plants for the treatment of sewage or trade effluents, or
- (g) has so abused in the opinion of the Central Government or as the case may be, of the State Government, his position as a member, as to render his continuance on the Board detrimental to the interest of the general public.

However, no order of removal shall be made by the Central Government or State Government unless the member concerned has been given reasonable opportunity of showing cause against the same.

### **Constitution of Joint Board**

Section 13 of the Act enables the constitution of Joint Boards by two or more Governments of contiguous States, or by the Central Government and one or more State Government contiguous to any Union Territory. The Joint Boards are to be constituted by an agreement. Section 14 of the Act provides for the following

composition of Joint Boards, constituted under agreement between two or more Governments of contiguous States, namely:

- (a) a full-time Chairman, being a person having special knowledge or practical experience in respect of matters relating to environmental protection or person having knowledge and experience in administering institutions dealing with the matters aforesaid, to be nominated by the Central Government;
- (b) two officials from each of the participating State to be nominated by the concerned participating State Government to represent that Government;
- (c) one person to be nominated by each of the participating State Governments from amongst the members of the local authorities functioning within the State concerned;
- (d) one non-official to be nominated by each of the participating State Governments to represent the interests of agriculture, fishery or industry or trade in the State concerned or any other interest which, in the opinion of the participating State Government, is to be represented;
- (e) two persons to be nominated by the Central Government to represent the companies or corporations owned, controlled or managed by the participating State Governments;
- (f) a full time member secretary having such qualifications, knowledge and experience of scientific, engineering or management aspects of pollution control to be appointed by the Central Government.

The Joint Board constituted by an agreement by the Central Government in respect of one or more Union Territory and one or more Governments of the State in the vicinity of such Union Territory or Union Territories, shall consists of the following members, namely:

- (a) a full-time Chairman, being a person having special knowledge or practical experience in respect of matters relating to environmental protection or person having knowledge and experience in administering institutions dealing with the matters aforesaid, to be nominated by the Central Government;
- (b) two officials to be nominated by the Central Government from the participating Union Territory or each of the participating Union Territories, as the case may be, and two officials to be nominated from the participating State or each of the participating States, as the case may be, by the concerned participating State Government;
- (c) one person to be nominated by the Central Government from amongst the members of the local authorities functioning within the participating Union Territory or each of the participating Union Territories, as the case may be, and one person to be nominated from amongst the members of the local authorities functioning within the participating State or each of the participating States, as the case may be, by the concerned participating State Government;
- (d) one non-official to be nominated by the Central Government and one person to be nominated by the participating State Government or State Governments to represent the interests of the agriculture, fishery, or industry or trade in the Union Territory or in each of the Union Territories or the State or in each of the States, as the case may be, or any interest which in the opinion of the Central Government or, as the case may be, of the State Government is to be represented;
- (e) two persons to be nominated by the Central Government to represent the companies or corporations owned, controlled or managed by the Central Government and situated in the participating Union Territory or Territories and two persons to be nominated by the Central

Government to represent the companies or corporations owned, controlled or managed by the participating State Governments;

- (f) a full time member secretary possessing qualifications, knowledge and experience of scientific, engineering or management aspects of pollution control to be appointed by the Central Government.

### **Special Provisions Relating to Giving of Directions**

Section 15 of the Act contains special provisions relating to giving of directions where Joint Boards have been constituted. Accordingly, the Government of the State for which the Joint Board is constituted, shall be competent to give any direction under the Act only in cases where such direction related to a matter within the exclusive territorial jurisdiction of the State and the Central Government alone shall be competent to give any direction under the Act where such directions relates to matters within the territorial jurisdiction of two or more States or pertaining to the Union Territory.

### **Functions of Central Board**

Section 16 of the Act specifically deals with functions of the Central Board. It empowers the Central Board to promote cleanliness of streams and wells in different areas of the States. Besides, the Central Board may perform all or any of the following functions, namely:

- (a) advise the Central Government on any matter concerning the prevention and control of water pollution;
- (b) co-ordinate the activities of the State Boards and resolve disputes among them;
- (c) provide technical assistance and guidance to the State Boards, carry out and sponsor investigations and research relating to problems of water pollution and prevention, control or abatement of water pollution;
- (d) plan and organise the training of persons engaged or to be engaged in programmes for the prevention, control or abatement of water pollution on such terms and conditions as the Central Board may specify;
- (e) organise through mass media a comprehensive programme regarding the prevention and control of water pollution;
- (f) collect, compile and publish technical and statistical data relating to water pollution and the measures devise for its effective prevention and control and prepare manuals, course or guides relating to retreatment and disposal of sewage and the trade effluents and disseminate information connected therewith;
- (g) lay down, modify or annul, in consultation with the State Government concerned, the standards for a stream or a well. However different standards may be laid down for the same stream or well or for different streams or wells having regard to the quality of water, flow characteristic of stream or well and the nature of the use of water in such stream or well or streams or wells;
- (h) plan and cause to be executed a nation-wide programme for prevention, control or abatement of water pollution;
- (i) perform such other functions as may be prescribed.

In addition, Central Board shall also perform such of the functions of the State Board as may be specified in an order made under Section 18(2). Under Section 18(2) the Central Government may direct the Central

Board to perform the functions of a State Board which had defaulted in complying with any directions given by the Central Government.

The Board is also empowered to establish or recognise a laboratory or laboratories to enable it to perform its functions efficiently, including the analysis of samples of water from any stream or well or of samples of any sewage or trade effluents.

### Functions of the State Board

The functions of the State Board as prescribed under Section 17 of the Act are:

- (a) to plan a comprehensive programme for the prevention, control or abatement of pollution of streams and wells in the State and to secure the execution thereof;
- (b) to advise the State Government on any matter concerning the prevention, control or abatement of water pollution;
- (c) to collect and disseminate information relating to water pollution and the prevention, control and abatement thereof;
- (d) to encourage, conduct and participate in investigations and research relating to problems of water pollution and prevention, control and abatement of water pollution;
- (e) to collaborate with the Central Board in organising the training of persons engaged or to be engaged in programmes relating to prevention, control or abatement of water pollution and to organise mass education programmes relating thereto;
- (f) to inspect sewage or trade effluents, works and plants for the treatment of sewage and trade effluents and to review plans, specifications or other data relating to plants set up for the treatment of water, works for the purification thereof and the system for the disposal of sewage or trade effluents or in connection with the grant of any consent as required by the Act;
- (g) to lay down, modify or annual effluent standards for the sewage and trade effluents and for the quality of receiving waters (not being water in an inter-State stream) resulting from the discharge of effluents and to classify waters of the State;
- (h) to evolve economical and reliable methods of treatment of sewage and trade effluents, having regard to the peculiar conditions of soils, climate and water resources of different regions and more especially the prevailing flow characteristics of water in stream and wells which render it impossible to attain even the minimum degree of dilution;
- (i) to evolve methods of utilisation of sewage and suitable trade effluents in agriculture;
- (j) to evolve efficient methods of disposal of sewage and trade effluents on land, as are necessary on account of the predominant conditions of scant stream flows that do not provide for major part of the year the minimum degree of dilution;
- (k) to lay down standards of treatment of sewage and trade effluents to be discharged into any particular stream taking into account the minimum fair whether dilution available in that stream and the tolerance limits of pollution permissible in the water of the stream, after the discharge of such effluents;
- (l) to make, vary or revoke any order:
  - (i) for the prevention, control and abatement of discharges of wastes into streams or wells;
  - (ii) requiring any persons concerned to construct new systems for the disposal of sewage and trade

- effluents or to modify, alter or extend any such existing system or to adopt such remedial measures as are necessary to prevent, control or abate water pollution;
- (m) to lay down effluent standards to be compiled with by persons while causing discharge of sewage or sullage or both and to lay down, modify or annual effluent standards for the sewage and trade effluents;
  - (n) to advise the State Government with respect to the location of any industry the carrying on of which is likely to pollute a stream or well;
  - (o) to perform such other functions as may be prescribed or as may, from time to time, be entrusted to it by the State Board or the State Government.

The Board may establish or recognise a laboratory or laboratories to enable the Board to perform its functions under this section efficiently, including the analysis of samples of water from any stream or well or of samples of any sewage or trade effluents.

In terms of Section 18 and in the performance of these functions the Central Board shall be bound by such directions in writing as the Central Government may give to it; and every State Board shall be bound by such directions in writing as the Central Board or the State Government may give to it. Where the direction given by the State Government is inconsistent with the direction given by the Central Board, that matter shall be referred to the Central Government for its decision.

Sub-sections (2), (3) and (4) of Section 18 provides that where the Central Government is of the opinion that any State Board had defaulted in complying with any direction given by the Central Board, it may direct the Central Board to perform any of the functions of the State Board. When the Central Board performs any of the functions of the State Board, the expenses incurred in connection therewith could be recovered by the Central Board with interest provided the State Board was entitled to so recover if it had performed the functions. Such expenses are recoverable as arrears of land revenue or of public demand.

### **Prevention and Control of Water Pollution**

Section 19 of the Act empowers the State Government to restrict the application of the Act to only such area or areas as may be declared in the notification published in the Official Gazette in this behalf. Each such Water Pollution Prevention and Control area may be declared either by reference to a map or by reference to a line of any water shed or boundary of any district or partly by one method and partly by another. The State Government has also powers to alter any Water Pollution Prevention and Control Area by way of extension or reduction, or define new Water Pollution Prevention and Control Area in which may be merged one or more Water Pollution Prevention and Control Areas or any parts thereof.

### **Power to Obtain Information**

Section 20 of the Act empowers the State Board or any officer empowered by it to make the survey of any area and gauge and keep records of flow or volume and other characteristics of any stream or well in such area and to take steps for the measurement and recording of the rain fall in such area or any part thereof and for the installation and maintenance for those purposes of gauges or other apparatus and works connected therewith and carry out stream surveys and take such other steps as may be necessary in order to obtain any required information.

The State Board has also been empowered to give directions to any person, who in its opinion is abstracting water from any such stream or well in the area in quantities which are substantial in relation to the flow or volume of that stream or well or is discharging sewage or trade effluent into any such stream or well, to give

such information as to the abstraction or discharge at such times and in such form as may be specified in the directions. With a view to preventing or controlling pollution of water the State Board may also give directions to any person in charge of any establishment where any industry operation or process or treatment and disposal system is carried on, to furnish to it information regarding the constructions, installation or operation of such establishment or of any disposal system or of any extension or addition thereto in such establishment and such other particulars as may be prescribed.

### **Power to Take Samples of Effluents**

Section 21 empowers the State Board or any officer authorised by it in this behalf to take for the purpose of analysis samples of water from any stream or well or samples of any sewage or trade effluent which is passing from any plant or vessel or from or over any place into any such stream or well. However, the result of any analysis of a sample of any sewage or trade effluent shall not be admissible in evidence in any legal proceedings unless the provisions of Sub-section (3), (4) and (5) are complied with.

Sub-section (3) says that when a sample (composite or otherwise as may be warranted by the process used) of any sewage or trade effluent is taken for analysis the person taking the sample shall:

- (a) serve on the person in charge of, or having control over, the plant or vessel or in occupation of the place (which person is hereinafter referred to as the occupier) or any agent of such occupier, a notice, then and there in such form as may be prescribed, of his intention to have it so analysed;
- (b) in the presence of the occupier or his agent divide the sample into two parts;
- (c) cause each part to be placed in a container which shall be marked, sealed and signed by both the person taking the sample and the occupier or his agent;
- (d) send one container forthwith to the laboratory established or recognised by the Central Board, in case such sample is taken from any area situated in the Union Territory, and in any other case, to the laboratory established or recognised by the State Board and
- (e) on the request of the occupier or his agent, send the second container to Central Water Laboratory in case such sample is taken from any area situated in the Union Territory and in any other case, to the State Water Laboratory.

When a sample of any sewage or trade effluent is taken for analysis and the person taking the sample serves on the occupier or his agent, a notice as required under clause (a) of Sub-section (3) and the occupier or his agent wilfully absent himself, then, the sample so taken shall be placed in a container which shall be marked, sealed and signed by the person taking the sample and the same shall be sent forthwith by such person for analysis to the prescribed laboratory and such person shall inform the Government analyst in writing about the wilful absence of the occupier or his agent.

In the case of a sample of sewage or trade effluent taken for analysis under Sub-section (1) and the person taking the sample serves on the occupier or his agent a notice under clause (a) of Sub-section (3) and the occupier or agent who is present at the time of taking the sample does not make a request for dividing a sample into two parts, then, the sample so taken shall be placed in a container, which shall be marked, sealed and signed by the person taking the sample and the same shall be sent forthwith by such person for analysis to the prescribed laboratory.

### **Report of Analysis of Samples**

Section 22 provides for the analysis of the samples, taken under Section 21, by the concerned Board analyst and submission of report of analysis to the concerned Board, in triplicate. On receipt of the report one copy

shall be sent to the occupier or his agent. Another copy shall be preserved for production in any court in any legal proceedings and the other copy shall be kept by the concerned Board. In the case of any inconsistency or discrepancy or variation in the results of analysis carried out by the laboratories established or recognised by the Central Board or the State Board, and that of laboratory established or specified under Section 51 or Section 52, the report of the latter laboratory shall prevail.

### **Power of Entry and Inspection**

Section 23 of the Act provides that any person empowered by the State Board in this behalf shall have a right at any time to enter with such assistance as he considers necessary, any place for the purpose of:

- (a) performing any of the functions of the Board entrusted to him;
- (b) determining whether and if so in what manner, any such functions are to be performed or whether any provision of the act or the rules made thereunder or any notice, order, direction or authorisation served, made, given or granted under the act is being or has been complied with;
- (c) examining any plant, record, register, document or any other material object or for conducting a search of any place in which he has reason to believe that an offence under this act or the rules made thereunder has been or is being or is about to be committed for seizing any such plant, record, register, document or other material object, if he has reason to believe that it may furnish evidence of the commission of an offence punishable under the act or the rules made thereunder.

However, these powers of inspection of a well, shall be exercised only at reasonable hours in a case where such well is situated in any premises used for residential purposes and the water thereof is used exclusively for domestic purposes.

The provisions of the Code of Criminal Procedure 1973 or any other corresponding law in force in any State in relation to which Cr. P.C. is not in operation, may apply as they apply to any search or seizure made under the authority of a warrant issued under Section 94 of the Cr. P.C. or as the case may be, under the corresponding law of the State.

### **Prohibition on Use of Stream or Well for Disposal of Polluting Matter**

Section 24 prohibits any person to knowingly cause or permit any poisonous, or noxious or polluting matter determined in accordance with such standards as may be laid down by the State Board to enter whether directly or indirectly into any stream or well, or sewer or on land. This section also prohibits any person to knowingly cause or permit to enter into any stream any other matter which may tend either directly or in combination with similar matters to impede the proper flow of water of the stream in a manner leading or likely to lead to a substantial aggravation of pollution due to other causes or of its consequences.

However, no person shall be guilty of an offence in respect of matters mentioned above by reason only of having done or caused to be done any of the following acts, namely:

- (i) constructing, improving or maintaining in or across or on the bank or bed of any stream any buildings, bridge, weir, dam, sluice, dock, pier, drain or sewer or other permanent works which he has a right to construct, improve or maintain;
- (ii) depositing any materials on the bank or in the bed of any stream for the purpose of reclaiming land or for supporting, repairing or protecting the bank or bed of such stream provided such materials are not capable of polluting such stream;
- (iii) putting into any stream any sand or gravel or other natural deposit which has flowed from or been deposited by current of such streams;

- (iv) causing or permitting, with the consent of the State Board, the deposit accumulated in a well, pond or reservoir to enter into any stream.

### Restriction on New Outlets and New Discharges

Section 25 of the Act which places certain restrictions on new outlets and new discharges is an important one. This section was extensively amended by the 1988 Amendment Act thereby making it obligatory on the part of a person to obtain the consent of the Board for establishing or taking any steps to establish any industry, operation or process which is likely to cause pollution of water and also empowering the Boards to limit their consents for suitable period so as to enable them to monitor observance of the prescribed conditions.

***Without the previous consent of the State Pollution Control Board no person is authorised to:***



- (i) establish or take any steps to establish any industry, operation or process or any treatment and disposal system or any extension or addition thereto which is likely to discharge sewage or trade effluent into a stream or well or sewer or on land;
- (ii) bring into use any new or altered outlet for discharge of sewage; or
- (iii) begin to make any new discharge of sewage or trade effluent.

The application for consent should be made in the specified form and manner accompanied by the prescribed fee. When an application for consent is received the State Board make such enquiry as it may deem fit. The procedure for making such enquiry is specified in the Rules framed by the State Government. While granting consent for establishment of any industry, operation etc. or for bringing into use any new or altered outlet, the Board may impose conditions as to the point of discharge of sewage or trade effluent. In the case of consent for new discharge, it may impose conditions as to the nature and composition, temperature, volume or rate of discharge of the effluent from the land or premises from which the discharge or new discharge is to be made. Such consent would be valid only for such period as may be specified in the order. The conditions imposed by the Board are binding on the person establishing or taking steps to establish any industry, operation or process or treatment and disposal system or extension or addition thereto or using the new or altered outlet or discharging the effluent from the land or premises.

The Board can also refuse to grant consent for reasons to be recorded in writing. Where without the consent of the Board any of the aforesaid acts like establishment of industry, operation, bringing into use outlet or effecting discharge of effluents etc. are done by any person, the Board may serve on the person concerned a notice imposing, such conditions as it might have imposed on an application for its consent in respect of such establishment outlet or discharge.

Section 18(6) obligates every State Board to maintain a register containing particulars of the conditions imposed. So much of the register as related to any outlet or to any effluent from any land or premises shall be open to inspection at all reasonable hours by any person interested in or affected by such outlet, land or premises as the case may be or by any person authorised by him in this behalf and the conditions so contained in such register shall be conclusive proof that the consent was granted subject to such conditions.

When an application for consent is made, the consent shall, unless given or refused earlier, be deemed to have been given unconditionally on the expiry of a period of four months of the making of the application.

'New or altered outlet has been defined to mean any outlet which is wholly or partly constructed on or after the commencement of the Act or which whether so constructed or not is substantially altered after such commencement. 'New discharge, means discharge which is not, as respects the nature and composition, temperature, volume and rate of discharge of the effluent substantially a continuation of a discharge made within the preceding twelve months (whether by the same or a different outlet) so however that a discharge which is in other respects a continuation of previous discharge made as aforesaid, shall not be deemed to be a new discharge by reason of any reduction of the temperature or volume or rate of discharge of the effluent as compared with the previous discharge.

### **Refusal or Withdrawal of Consent by a State Board**

Section 27 empowers a State Board to grant or refuse to grant its consent for the establishment of any industry, operation or process or treatment and disposal system or extension or addition thereto or to the bringing into use of a new or altered outlet, unless the industry, operation or process or treatment and disposal system or extension/addition thereto or the outlet is so established as to comply with the conditions imposed by the Board, in order to enable it to exercise its right to take samples of the effluent. A State Board is also empowered to review any condition imposed under Section 25 or Section 26 and may serve on the person to whom consent under these sections had been granted, a notice, making any reasonable variation of or revoking any such condition. The refusal of any consent can also be reviewed by the Board. Where any variation is made of the conditions, such conditions shall continue to be in force until revoked by the Board.

### **Appeal**

Section 28 of the Act deals with appeals and entitles any person aggrieved by an order of the State Board to prefer an appeal with such appellate authority as the State Government may constitute within 30 days from the date on which the order is communicated to him. The Appellate Authority may extend time for filing an appeal if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal in time. The Appellate Authority after giving the appellant and the State Board an opportunity of being heard, shall dispose of the appeal as expeditiously as possible. The appellate authority may direct annulment or substitution of any unreasonable condition imposed by the State Board.

### **Power of the State Board to Carry Out Certain Works**

When the State Board imposes any conditions while granting consent under Section 25 or Section 26 and such conditions require the person concerned to execute any work in connection therewith, but the person fails to execute the same within the specified time, then the Board may serve a notice requiring the person to execute the specified work within prescribed time. Such time shall not be less than thirty days. If in spite of such notice the person fails to execute the work, then after the expiration of the time specified in the notice, the Board itself may execute or cause to be executed such work. All expenses incurred by the Board for execution of the work, together with interest, could be recovered as arrears of land revenue or of public demand.

### **Furnishing of Information to State Board and other Agencies**

Section 31 requires the person incharge of any place where any industry, operation, or process or any treatment and disposal system or any extension or addition thereto is being carried on, to intimate to the State Board or any prescribed authority/agency the occurrence of any accident or other unforeseen act or event as a result of which any poisonous, noxious or polluting matter is being discharged, or is likely to be discharged in such stream or well or sewer or on land and as a result of such discharge, the water in such stream or well being polluted or is likely to be polluted. The provisions of this section are also applicable to any local authority which operates any sewage system or sewage works.

**What are the Emergency Measures taken by State Board in Case of Pollution of Stream or Well?**

Section 32 empowers the State Board to take certain emergency measures. Accordingly where it appears to the State Board that any poisonous, noxious or polluting matter is present in any stream or well or on land by reason of the discharge of such matter in such stream or well or on land, or has entered into that stream or well due to any accident or unforeseen act or event, and the Board is of the opinion that it is necessary or expedient to take immediate action, then it may for reasons to be recorded in writing, carry out such operations as it may consider necessary for all or any of the following purposes, namely:



- (a) removing that matter from stream or well and disposing it of in such manner as the Board considers appropriate;
- (b) remedying or mitigating any pollution caused by its presence in the stream or well,
- (c) issuing orders immediately restraining or prohibiting the person concerned from discharging any poisonous, noxious or polluting matter into the stream or well or on land or from making insanitary use of the stream or well.

**Boards Power to Make Application to Courts**

Section 33 of the Act deals with the power of Board to make application to Courts for restraining apprehended pollution of water in streams or wells.

Where it is apprehended by a Board that the water in any stream or well is likely to be polluted by reason of the disposal or likely disposal of any matter in such stream or well or in any sewer or on any land or otherwise, the Board may make an application to the court, not inferior to that of a Metropolitan Magistrate or Judicial Magistrate of the first class, for restraining the person from so causing the pollution. On receipt of an application the court may make such order as it deems fit. Where the court makes an order restraining any person from polluting the water in any stream or well, it may direct the person who is likely to cause or has caused the pollution of the water in the stream or well, to desist from taking such action as is likely to cause pollution or, as the case may be, to remove from such stream or well, such matter. The Court may also authorise the Board, if the direction particularly in respect of removal of any matter from such stream or well has not been complied with by the person to whom such direction is issued, to undertake the removal and disposal of the matter in such manner as may be specified by the court.

All expenses incurred by the Board in removing any matter in pursuance of the authorisation or in the disposal of any such matter may be defrayed out of any money obtained by the Board from such disposal and any balance outstanding shall be recoverable from the person concerned as arrears of land revenue or of public demand.

**Power to Give Directions**



Section 33A introduced by the 1988 Amendment Act is a very important provision whereunder the Board has been empowered to give directions including that of closure of an offending industry. Under this section which has overriding effect over other law, and subject to the directions that may be given by the Central Government, a Board may in the exercise of its powers and performance of its functions, issue directions in writing to any person, officer or authority including a direction for the closure, prohibition, regulation of any industry, operation or process or a direction for the stoppage or regulation of supply of electricity, water or any other service. The person or authority to whom such directions are issued is bound

*to comply with the same.*

## **Penalties and Procedure**

Chapter VII of the Act contains provisions relating to penalties and procedure. Under Section 41 failure to comply with the directions given under Section 20(2) (Information about abstraction of water or discharge of effluence) or Section 20(3) (Information regarding construction, installation or operation of any establishment of or any disposal system etc.) within the time specified in the direction, would on conviction, be punishable with imprisonment for three months or with fine upto ₹10,000 or with both. Where the failure continues, a fine of ₹5,000 for each such day of continuance is also leviable.

Failure to comply with an order issued under Section 31(l)(c) (restraint or prohibition from discharging poisonous, noxious or polluting matter into stream or well or on land); or any direction issued by court under Section 33(2) (directing any person from desisting from causing any pollution of the water in any stream or well etc.); or any direction issued under Section 33A (direction regarding closure, regulation, stoppage of electricity etc.) is also punishable on conviction, with imprisonment for a period ranging from eighteen months to six years and with fine. Continuing contravention attracts an additional fine of ₹5,000 for each day after the conviction for the first such offence. Where such failure continues beyond one year the offender can be punished with imprisonment for a period of two to seven years and with fine also.

In terms of Section 42, whoever does the following acts shall be liable to imprisonment for a period of three months or fine upto ₹10,000 or with both:

- (i) destroys, pulls down, removes, injures or defaces any pillar, post, or stake fixed in the ground or any notice or other matter put up, inscribed, or placed by or under the authority of the Board; or
- (ii) obstructs any person acting under the orders or directions of the Board from exercising his powers and performing his functions under the Act; or
- (iii) damages any works or property belonging to the Board;
- (iv) fails to furnish to any officer or other employee of the Board any information;
- (v) fails to intimate the occurrence of any accident or other unforeseen act or event to the Board or other authorities or agencies;
- (vi) makes false statement knowingly or wilfully in giving any information which he is required to give or for obtaining the consent from the Board under the Act.

Contravention of the provisions of Section 24 (Prohibition or use of stream or well for disposal of polluting matter), Section 25 (Restrictions on new outlets and new discharges) and Section 26 (consent for operating existing discharge outlets etc.) attracts imprisonment ranging from eighteen months to six years and also fine.

Section 45 of the Act specifies that if any person convicted of any offence under Section 24 or Section 25 or Section 26 is again found guilty of an offence involving a contravention of the same provision, he shall on the second and on every subsequent conviction be punishable with imprisonment for a term which shall not be less than one and half year but may extend to six years and with fine. But no cognizance shall be taken of any conviction made more than two years before the commission of the offence which is being punished.

Contravention of any provision of the Act or order or direction issued thereunder for which no penalty is provided in the Act, is punishable with imprisonment for a period upto three months and with fine upto

₹10,000. Continuing contravention attracts a penalty of ₹5,000 for each day default after the first contravention.

### Offences by Companies

Section 47 of the Act provides that where an offence has been committed by a company, every person who at the time the offence was committed was in charge of, and was responsible to the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. However, if any such person proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence, he shall not be liable to punishment. Where an offence has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Section 48 of the Act provides that where the offence under the Act has been committed by any Department of Government, the Head of the Department shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. But the head of the Department shall not be liable to punishment if he proves that the offence was committed without his knowledge or that he exercised due diligence to prevent commission of such offence.

### Power to Supersede the Board

Section 61 of the Act empowers the Central Government to supersede the Central Board and the Joint Boards under certain circumstances. Similarly, under Section 62, State Government has been empowered to supersede the State Boards under following circumstances:

- (i) the Board concerned has persistently made default in the performances of the functions imposed on it by or under the Act; or
- (ii) circumstances exist which render it necessary in the public interest to so supersede the Board.

### Water (Prevention and Control of Pollution) Cess Act, 1977

With a view to augment the resources of the Central Board and the State Boards for the prevention and control of water pollution, the Water (Prevention and Control of Pollution) Cess Act, 1977 has been brought on the statute book. This Act authorises the levy and collection of a cess on water consumed by person carrying on certain industries and by local authorities. The object of the Cess Act is to ensure that the State or Central Boards are able to raise sufficient finance other than the funds that are being contributed by the Central Government and States and also by way of gifts and donations, in the effective discharge of functions contemplated under the Pollution Control Laws.

### LESSON ROUND UP

- Water (Prevention and Control of Pollution) Act, 1974 has been enacted to provide for the prevention and control of water pollution and maintaining or restoring wholesomeness of water, for the establishment of Boards, with a view to carrying out these purposes, for the prevention and control of water pollution, for conferring on and assigning to such Boards powers and functions relating thereto and for matters connected therewith.
- Water (Prevention And Control of Pollution) Act, 1974 empowers the Central Government to constitute a Central Pollution Control Board to exercise such powers and functions as may be conferred upon it.

- Water (Prevention And Control of Pollution) Act, 1974 empowers the State Government to constitute the State Boards.
  - Water (Prevention And Control of Pollution) Act, 1974 empowers the State Government to restrict the application of the Act to only such area or areas as may be declared in the notification published in the Official Gazette in this behalf.
  - Water (Prevention And Control of Pollution) Act, 1974 empowers the State Board to take certain emergency measures.
  - Board may in the exercise of its powers and performance of its functions, issue directions in writing to any person, officer or authority including a direction for the closure, prohibition, regulation of any industry, operation or process or a direction for the stoppage or regulation of supply of electricity, water or any other service.

## **SELF TEST QUESTIONS**

1. What are the provisions relating to prevention and control of water pollution?
  2. Discuss briefly the restriction on new outlets and new discharges under the Water (Prevention and Control of Pollution) Act.
  3. Write note on the following:
    - (i) Restrictions on use of certain Industrial Plants.
    - (ii) Powers to take samples of effluents.
  4. What are the powers of State Boards in taking samples?
  5. What are the disqualifications of a person to be a member of State Pollution Control Board?

# Lesson 15

## LAW RELATING TO REGISTRATION OF DOCUMENTS

### LESSON OUTLINE

- Registrable Documents
- Documents whose registration is compulsory
- Documents of which registration is optional
- Time-limit for presentation
- Re-registration of documents
- Documents executed out of India
- Presentation of a will for registration
- Presenting of documents for registration
- Registered document when operative
- Effect of non-registration of documents
- Certificate of registration
- Procedure after registration
- Appeal to registrar
- Application to registration
- Procedure before the registrar
- Order by registrar
- Institution of suit
- Exemption of certain documents executed by or in favour of Government

### LEARNING OBJECTIVES

Registration means recording of the contents of a document with a Registering Officer and preservation of copies of the original document. Document whose registration is compulsory are instruments of gift of immovable property; other non-testamentary instruments which purport or operate to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent, of the value of one hundred rupees, and upwards, to or in immovable property; leases of immovable property from year to year, or for any term exceeding one year, or reserving a yearly rent and non-testamentary instruments transferring or assigning any decree or order of a court or any award when such decree or order or award purports or operates to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent, of the value of one hundred rupees and upwards, to or in immovable property.

The Registration Act, 1908 is the law relating to registration of documents. The object and purpose of the Act among other things is to give information to people regarding legal rights and obligations arising or affecting a particular property, and to perpetuate documents which may afterwards be of legal importance, and also to prevent fraud.

It is important for the students to be thoroughly acclimatized with this branch of law to know its practical significance.

## INTRODUCTION

Registration of a document *inter alia*, ensures its proper preservation and record. The Registration Act, 1908 is the law relating to registration of documents. Registration is of a *document* and not of a transaction.

## REGISTERABLE DOCUMENTS

Documents can be classified into two classes:

- (i) Those whose registration is compulsory; (Section 17)
- (ii) Those whose registration is optional. (Section 18)

## DOCUMENTS WHOSE REGISTRATION IS COMPULSORY

According to Section 17 of the Registration Act, 1908, documents whose registration is compulsory are the following:

*(a) Instruments of gift of immovable property*

In a case where the donor dies before registration, the document may be presented for registration after his death and if registered it will have the same effect as registration in his life time. On registration the deed of gift operates as from the date of execution.



**It was held by the Privy Council in *Kalyana Sundram v. Karuppa*, AIR 1927 PC 42, that while registration is a necessary solemnity for the enforcement of a gift of immovable property, it does not suspend the gift until registration actually takes place, when the instrument of gift has been handed over by the donor to the donee and accepted by him, the former has done everything in his power to complete the donation and to make it effective. And if it is presented by a person having necessary interest within the prescribed period the Registrar must register it. Neither death nor the express revocation by the donor, is a ground for refusing registration, provided other conditions are complied with. (Cf. Mulla Registration Act (1998), page 36)**

(b) Other non-testamentary instruments (other than instruments of gift of immovable property) which purport or operate to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest whether vested or contingent, of the value of one hundred rupees and upwards, to or in immovable property situated in a district in which this Act is in force.

A document which is plainly intended to be operative immediately is non-testamentary (*Umrao Singh v. Lachhman*, (1911) 1 LR 33 All 344, 355 (PC); Mulla, Registration Act (1998), page 40).

Description of a document as a will does not make it a will (*Tirugnannpal v. Poonamma*, AIR 1921 PC 89).

The expressions "create", "assign", "limit" or "extinguish" imply a definite change of legal relation to a property by an expression of will embodied in the document. It implies a declaration of will.

The expression "declare" (as used in Section 17) has also to be interpreted on the same lines. It does not mean a mere declaration of fact, but connotes a writing effectuating a change of relation (*Bageshwari Charan v. Jagarnath Kuare*, AIR 1932 PC 55; Mulla, Registration Act (1998), page 41).

Whether an instrument requires registration under Section 17(1)(b) depends upon whether it operates or

purports to bring about a change in legal relation in respect of some property. For purposes of Section 17(1)(b) a distinction should be drawn between (i) a right in or to property and (ii) such rights as are merely incidental to the ownership of property and are really in the nature of powers or options which every owner is free to exercise in dealing with his property in a particular way. The latter may be described as rights in relation to the property, but strictly speaking, they are not rights in or to property. Generally, when a right in or to property is assigned, created, declared, limited or extinguished, then there must be a definite change of legal relation to the property.

(c) Non-testamentary instruments which acknowledge the receipt or payment of any consideration on account of the creation, declaration, assignment, limitation, or extinction of any such right, title or interest.

This clause requires an acknowledgement in the form of a receipt to be registered, but not an acknowledgement of the fact that a transaction has taken place. To be registrable under this clause a receipt must satisfy the following two conditions:

- (i) it must be the receipt of a consideration; and
- (ii) it must on the face of it be an acknowledgement of payment or some consideration on account of the creation, declaration, assignment, limitation or extinction of an interest of the value of ₹100 or upwards in immovable property.

The receipt must be such as to be linked with the creation etc. of a right. A mere acknowledgement of payment is not compulsorily registrable.

### **Illustration**

In a suit by *A* against *B* for lands, *B* pleads adverse possession. *B* in defence, proves *B*'s acknowledgement (in a petition to the Collector) that the gift is in her favour. The petition is not admissible and does not require registration (Mulla, Registration Act (1998), page 69; *Bageshwari v. Jagarnath Kuare*, AIR 1932 PC 55).



**Delay in registration of a gift does not postpone its operation.** Section 123, Transfer of Property Act, 1882 merely requires that donor should have signed the deed of gift. Hence a gift deed can be registered even if the donor does not agree to its registration (*Kalyan Sundaram Pillai v. Karuppa Mopanar*, AIR 1927 PC 42; *Venkata Rama Reddy v. Pillai Rama Reddy*, AIR 1923 Mad. 282).

A lease for one year containing an option to the tenant to renew for a further period of one year or any other term is not a lease for a term exceeding one year, and does not require registration under this clause. Under Section 107 of the Transfer of Property Act, a lease of one year or reserving a yearly rent can be made only by a registered instrument. But where the lease is only for one year with a reserved rent for the period for which it has been granted, viz. one year, it does not require registration.

### **Cases under Section 107 of Transfer of Property Act, and Section 17(1)(d) of Registration Act**

A comparison of both these Sections would show that a lease of immovable property is compulsory registrable:

- (a) if it is from year to year; or
- (b) if it is for a term exceeding one year; or

- (c) if it reserves a yearly rent.

If a lease is of a very high value but is neither from year to year, nor for any term exceeding one year, nor reserving a yearly rent, it does not require registration under Section 17(1)(d).

- (d) Non-testamentary instruments transferring or assigning any decree or order of a Court or any award in order to create interests as mentioned in Clause (b).

A transfer of a decree or order of a court or of any award when such decree or order or award operates to create, declare, etc. any interest of the value of ₹100 and upwards in immovable property, requires registration.

However, the State Government is empowered to exempt any leases executed which do not exceed five years and the annual rents reserved which do not exceed 50 rupees, from the operation of this Sub-section.

- (e) It may be pointed out that the documents containing contracts to transfer for consideration, any immovable property for the purpose of Section 53A of the Transfer of Property Act, 1882 shall be registered if they have been executed on or after the commencement of the Registration and other Related Laws (Amendment) Act, 2001 and if such documents are not registered on or after such commencement, then they shall have no effect for the purposes of the said Section 53A.

### **Exceptions to Section 17(1)**

The registration of the non-testamentary documents mentioned in clauses (b) and (c) of Section 17(1) is subject to the exceptions provided in Sub-section (2) of Section 17. These are as follows:

- (i) any composition deed, i.e., every deed the essence of which is composition; or
- (ii) any instrument relating to shares in Joint Stock Company; or
- (iii) any debentures issued by any such Company; or
- (iv) any endorsement upon or transfer of any debenture; or
- (v) any document other than the documents specified under clause (e) above creating merely a right to obtain another document which will, when executed create, declare, assign, limit or extinguish any such right, title or interest; or
- (vi) any decree or order of a court; or
- (vii) any grant of immovable property by the Government; or
- (viii) any instrument of partition made by Revenue-officer; or
- (ix) any order granting a loan or instrument of collateral security granted under the Land Improvement Act, 1871, or the Land Improvement Loans Act, 1883; or
- (x) any order granting loan made under the Agriculturists Loans Act, 1884 or instrument for securing the repayment of a loan made under that Act; or
- (xi) any order made under the Charitable Endowments Act, 1890 vesting any property in a treasurer of a charitable endowment or divesting any such Treasurer of any property; or
- (xii) any endorsement on a mortgage deed acknowledging the payment of the whole or any part of the mortgage money, and any other receipt for payment of money, due under a mortgage when the receipt does not purport to extinguish the mortgage; or
- (xiii) any certificate of sale granted to the purchaser of any property sold by public auction by Civil or Revenue Officer.

**Explanation:**

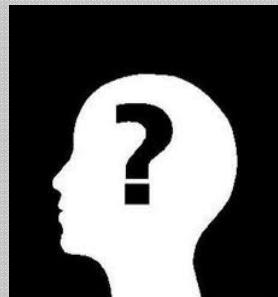
A document purporting or operating to effect a contract for the sale of immovable property shall not be deemed to require for ever to have required registration by reason only of the fact that such document contains a recital of payment of any earnest money or of the whole or any part of the purchase money.

**Test your knowledge****State whether the following statement is “True” or “False”**

*A mere acknowledgement of payment is always registrable.*

- *True*
- *False*

**Correct Answer: False**

**DOCUMENTS OF WHICH REGISTRATION IS OPTIONAL**

Whereas Section 17 of the Act has made registration of certain documents compulsory, Section 18 specifies documents, registration of which is optional. It provides that any of the following documents may be registered under this Act, namely:

- (a) instruments (other than instruments of gift and wills) which purport or operate to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest whether vested or contingent, of value less than one hundred rupees, to or in immovable property;
- (b) instruments acknowledging the receipt or payment of any consideration on account of the creation, declaration, assignment; limitation or extinction of any such right, title or interest;
- (c) leases of immovable property for any term not exceeding one year and leases exempted under Section 17;
- (d) instruments transferring or assigning any decree or order of a court or any award when such decree or order or award purports or operates to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent of a value less than one hundred rupees, to or in immovable property;
- (e) instruments (other than wills) which purport or operate to create declare, assign, limit or extinguish any right, title or interest to or in movable property;
- (f) wills; and
- (g) other documents not required by Section 17 to be registered. (Section 18)

**TIME LIMIT FOR PRESENTATION**

**A document other than a will must be presented within four months of its execution. In cases of urgent necessity, etc. the period is eight months, but higher fee has to be paid (Sections 23-26). These limits are mandatory (*Ram Singh v. Jasmer Singh*, AIR 1963 Punj. 100). If delay is due to act of Court, it has to be disregarded (*Raj Kumar v. Tarapa*, AIR 1987 SC 2195).**

Section 23, proviso prescribes a period of four months for presenting a copy of a decree or order. It is counted from the date of the decree.

### Unstamped document

If the document is not sufficiently stamped its presentation is still good presentation though penalty under the Stamp Act can be levied (*Mahaliram v. Upendra Nath*, AIR 1960 Pat 470).

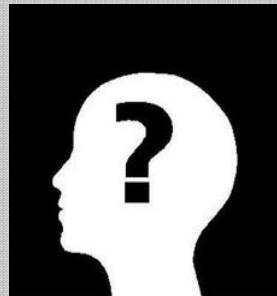
### Test your knowledge

#### **State whether the following statement is “True” or “False”**

*According to Section 17, registration of instruments of gift of immovable property is compulsory.*

- *True*
- *False*

**Correct Answer: True**



### RE-REGISTRATION

Section 23A provides for the re-registration of certain documents. The section is mainly intended to deal with situations where the original presentation was by a person not duly authorised. It overrides the decision in *Jambu Prasad v. Mohammed Aftab Ali Khan*, (1914) ILR 37 All 49).

### SEVERAL EXECUTANTS

Under Section 24 a document executed by several persons at different times may be presented for registration and re-registration within four months from the date of each execution.

The registration is “partial” in regard to each party. (Mulla, Registration Act (1998), page 163)

### DOCUMENTS EXECUTED OUT OF INDIA

As per Section 26 Where the registering officer is satisfied that the document was executed outside India and it has been presented for registration within four months after its arrival in India, he may accept such document for registration on payment of proper registration fee. **A document executed outside India is not valid unless it is registered in India (*Nainsukhdas v. Gowardhandas*, AIR 1948 Nag. 110).**

Incidentally, Section 26 indicates that the Act applies to ex-India documents relating to property in India. (Mulla, page 166)

### PRESENTATION OF A WILL

Section 27 provides that a *will* may be presented for registration at any time or deposited in a manner provided in Sections 40-46. Registration of a will is optional under Section 18(e).

### PLACE OF REGISTRATION

Section 28 provides that documents affecting immovable property mentioned in Sections 17(1) and (2) and Sections 17(1)(a)(b)(c) and (cc)(d) and (e), Section 17(2), etc. shall be presented for registration in the office of a Sub-Registrar within whose sub-district the whole *or some portion* of the relevant property is situated and any other document may be presented for registration either in the office of the Sub-Registrar in whose

sub-district the document was executed or in the office of any other Sub-Registrar under the State Government at which all the persons executing desire the document to be registered. (All these documents relate to immovable property). Registration of a document elsewhere has been held to be void (*Harendra Lal Roy Chowdhuri v. Hari Dasi Debi*, (1914) ILR 41 Cal. 972, 988 (PC); Mulla, Registration Act (1998), page 167 and cases in footnote 2).

There is nothing in law to prohibit a person conveying property in one district and residing and owing property in another district and asking the vendee to accept a conveyance also of some small property in the district in which he resides, so that the sale-deed may be registered there and he may not be put to the trouble and expense of a journey to the other district. It is not correct to say in such a case that the sale-deed is not validly registered at the place where it is got registered.

However, there should be no fraud or collusion. Smallness of the area does not necessarily lead to inference of fraud. (Mulla Registration Act (1998), pages 169-171. See in particular the cases cited in Mulla page 170, footnotes 15-19).

### COPY OF A DECREE OR ORDER

A copy of a decree or order may be registered with the Sub-Registrar within whose sub-district it was made. If the decree or order does not affect immovable property, it may be presented for registration in the office of any other Sub-Registrar under the State Government at whose office all persons claiming under the decree or order desire it to be registered.

### REGISTRATION IN CERTAIN CITIES

In any city comprising a Presidency town or in Delhi, a document relating to property situated anywhere in India may be registered (Section 30). Delhi was added by Amendment Act 45 of 1969.

Under Section 31, registration is permitted in cases of necessity under extra-ordinary circumstances, at the residence of the executant.

### PRESENTING OF DOCUMENTS FOR REGISTRATION

Section 32 specifies the persons who can present documents for registration at the proper registration office. Such persons are as follows:

- (a) some person executing or claiming under the same, or in the case of a copy of a decree or order, claiming under the decree or order, or
- (b) the representative or assign of such person, or
- (c) the agent of such person, representative or assign, duly authorised by power-of-attorney executed and authenticated in the manner hereinafter mentioned.

**It is immaterial whether the registration is compulsory or optional; but, if it is presented for registration by a person other than a party not mentioned in Section 32, such presentation is wholly inoperative and the registration of such a document is void (*Kishore Chandra Singh v. Ganesh Prashad Singh*, AIR 1954 SC 316).** However, Sections 31, 88 and 89 provide exceptions to this requirement.

For the purpose of Section 32, a special power of attorney is required as provided under Section 33. A general power of attorney will not do. Section 33 requires that a power of attorney, in order to be recognised as giving authority to the agent to get the document registered, should be executed before and then authenticated by the Registrar within whose district or sub-district the principal resides. (Sections 32 to 35)

## ENQUIRY BEFORE REGISTRATION BY REGISTERING OFFICER

For registering a document the persons executing such document or their representatives, assigns or authorised agents must appear before the registering officer within the time allowed for presentation. (Section 34)

In Section 34, the expression “person executing” not only includes the agent who has signed (with authority), but also the principal who is a party (*Puran Chand v. Manmotha Nath*, AIR 1928 PC 38).

It is the compliance with the provisions of Sections 34, 35, 58 and 59 of the Act, which really constitutes registration and not the presence of the certificate. Hence, subsequent acts of the Registrar which are ministerial acts, cannot affect the validity of the registration and the absence of final certificate of registration under section 60 cannot affect its validity.

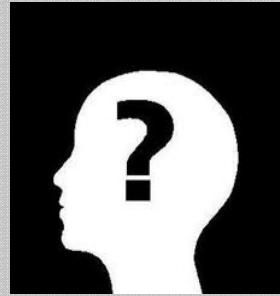
### Test your knowledge

**State whether the following statement is “True” or “False”**

*A document executed outside India can be valid even if it is not registered in India.*

- *True*
- *False*

**Correct Answer: False**



## PRESENTING WILLS AND AUTHORITIES TO ADOPT

### (a) Who is entitled to present Wills and authorises to adopt

The testator, or after his death, any person claiming as executor or otherwise under a will, may present it to any Registrar or Sub-Registrar for registration. In case of authority for adoption, the donor or (after his death) the donee, or any authority to adopt, or the adoptive son, may present it to any Registrar or Sub-Registrar for registration. (Section 40) Thus, even a legatee can present a will (*Venkatapayya v. Venkata Ranga*, AIR 1929 PC 24).

### (b) Registration of will and authority to adopt

- (i) A will, or an authority to adopt, if presented by the testator or the donor, may be registered in the same manner as any other document. [Section 41(1)]
- (ii) If presented by any other person entitled to present it, it shall be registered if the registering officer is satisfied about the particulars mentioned in Section 41(2).

## DEPOSIT OF WILLS

Any testator may, either personally or by duly authorised agent, deposit with any Registrar his will in a sealed cover superscribed with the name of the testator and that of his agent, if any, and with a statement of the nature of the document.

On receiving such documents, the Registrar on being satisfied shall transcribe in his Registrar Book No. 5, the superscription and shall note the date, time, month, etc. of such receipt and shall then place and retain the sealed cover in his fire-proof box.

However, the testator may withdraw it by applying for the same and the Registrar shall deliver it accordingly (Sections 42 to 46).

### REGISTERED DOCUMENT WHEN OPERATIVE

(a) A registered document shall operate from the time from which it would have commenced to operate if no registration thereof had been required or made and not from the time of its registration. (Section 47)

(b) As between two registered documents, the date of execution determines the priority. Of the two registered documents, executed by same persons in respect of the same property to two different persons at two different times, the one which is executed first gets priority over the other, although the former deed is registered subsequently to the later one (*K.J. Nathan v. S.V. Maruthi Rai*, AIR 1965 SC 430; Mulla page 207).

In effect<sup>1</sup> Section 47 means that a document operates from the date of execution (as between the parties). (Mulla, Registration Act (1998), pages 207, 209)

### REGISTERED DOCUMENT RELATING TO PRIORITY WHEN TO TAKE EFFECT AGAINST ORAL AGREEMENT

Generally, priority to rights accorded by different transfers is governed by the principles embodied in the maxim *qui prior tempore potior est jure* that is “he who is first in time is better in law”. But this general rule is subject to exceptions created by Sections 48 and 50. Section 48 refers to the priority of the registered agreements over oral agreements and Section 50 refers to the priority of registered agreements over non-registered agreements. (Section 48)

#### Notice

In spite of the explicit wording of Section 48, it has for long time been held, that a subsequent registered deed will not prevail over a prior unregistered deed or a prior oral transaction if the subsequent transferee had notice of the prior transaction. (Mulla Registration Act (1998), pages 215-216)

### EFFECT OF NON-REGISTRATION OF DOCUMENTS REQUIRED TO BE REGISTERED

Section 49 of the Act provides that no document required by Section 17 or by any provision of the Transfer of Property Act, 1882 to be registered shall:

- (a) affect any immovable property comprised therein; or
- (b) confer any power to adopt; or
- (c) be received as evidence of any transaction affecting such property or conferring such power *unless it has been registered*.

Section 49 is mandatory, and a document which is required to be registered cannot be received in evidence as affecting immovable property. (Mulla, pages 223 to 228)

An unregistered document which comes within Section 17 cannot be used in any legal proceeding to bring out indirectly the effect which it would have if registered.

However, as provided in Section 49, proviso, an unregistered document affecting immovable property and required by this Act or the Transfer of property Act, 1882 to be registered may be received as evidence of a contract in a suit for specific performance or as evidence of part performance of a contract for the purposes of Section 53A of the Transfer of Property Act, 1882 or as evidence of any collateral transaction not to be effective

<sup>1</sup> Section 47 does not affect rules of personal law requiring possession. [Mulla (1998), page 209].

by registered instrument. All that the proviso to Section 49 permits is that in a suit for specific performance an unregistered document affecting immovable property may be given in evidence. The purpose is that the document which has not conveyed or passed title may still be used as evidence of the terms.

**In *In K. Narasimha Rao v. Sai Vishnu*, AIR 2006 NOC (A.P.) p. 80, it has been held that It is settled legal principle that an unstamped instrument is not at all admissible in evidence even for collateral purpose. But an unregistered instrument originally unstamped, if duly stamped subsequently can be admitted in evidence even though it continues to be unregistered for collateral purpose but actual terms of transaction cannot be looked into. In instant case, however settlement deed in question produced by defendant was not only unregistered but also insufficiently stamped. That apart on an objection raised by plaintiff, Court had already passed an order directing impounding of document, which was never complied with by defendant. In such circumstances, document in question, which still remained insufficiently stamped could not be admitted in evidence even for collateral purpose. Application filed by defendant seeking to admit said document for collateral purpose is liable to be dismissed.**

### **REGISTERED DOCUMENTS RELATING TO PROPERTY WHEN TO TAKE EFFECT AGAINST ORAL AGREEMENT**

Registered documents relating to any property whether movable or immovable shall take effect against any oral agreements or declaration relating to such property unless followed by delivery of possession which constitutes a valid transfer under any law for the time being in force. (Section 48)

### **CERTAIN REGISTERED DOCUMENTS RELATING TO LAND WHICH WILL TAKE EFFECT AGAINST UNREGISTERED DOCUMENTS**

Section 50 provides as under:

- (1) Every document of the kinds mentioned in clause (a), (b), (c) and (d) of Section 17, Sub-section (1) and clauses (a) and (b) of Section 18, shall if duly registered, take effect as regards the property, comprised therein, against every unregistered document relating to the same property, and not being a decree or order, whether such unregistered document be of the same nature as the registered document or not.
- (2) Nothing in Sub-section (1) applies to leases exempted under the proviso to Sub-section (1) of Section 17 or to any document mentioned in Sub-section (2) of the same section or to any registered document which had no priority under the law in force at the commencement of this Act.

### **Test your knowledge**

#### **Choose the correct answer**

*Which of the following section mainly deals with situation when the original presentation is made by a person not duly authorized?*

- (a) Section 27
- (b) Section 23A
- (c) Section 17(1)
- (d) Section 26

**Correct Answer: (b)**



## MISCELLANEOUS PROVISIONS

### Duties and powers of registering officer

The following books must be kept in the several offices as follows:

A – In all Registration Offices

Book 1 – “Register of non-testamentary documents relating to immovable property”;

Book 2 – “Record of reasons for refusal to register”;

Book 3 – “Register of wills and authorities to adopt”;

Book 4 – “Miscellaneous Register”;

B – In the Offices of Registrars

Book 5 – “Register of deposits of Wills”.

(2) In Book 1 shall be entered or filed all documents or memorandum registered under Sections 17, 18 and 89 which relate to immovable property, and are not *wills*.

(3) In Book 4 shall be entered all documents registered under clauses (d) and (f) of Section 18 which do not relate to immovable property.

The registering officer should enter the registration in the proper book. However, if by mistake and in good faith the registration was entered in the wrong book, it will not make the registration invalid.

When the document is presented for registration, the day, hour and place of presentation and signature of every person presenting it shall be endorsed.

The registering officer should give a receipt for such document to the person presenting it and shall make a copy of the document in the appropriate book.

All such books shall be authenticated from time to time as prescribed by the Inspector General. (Sections 51 to 57)

## PROCEDURE ON ADMISSION TO REGISTRATION

### **Particulars to be endorsed on documents admitted to registration :**

(1) On every document admitted to registration, other than a copy of a decree or order, or a copy sent to a registering officer under Section 89, there shall be endorsed from time to time the following particulars, namely:

(a) the signature and addition of every person admitting the execution of the document and, if such execution has been admitted by the representative, assign or agent of any person, the signature and addition of such representative, assign or agent;

(b) the signature and addition of every person examined in reference to such document under any of the provisions of this Act; and

(c) any payment of money or delivery of goods made in the presence of the registering officer in reference to the execution of the document and any admission of receipt of consideration, whole or in part, made in his presence in reference to such execution.

(2) If any person admitting the execution of a document refuses to endorse the same, the registering

officer shall nevertheless register it, but shall at the same time endorse a note of such refusal. (Sections 58 to 62)

## **CERTIFICATE OF REGISTRATION**

- (a) After the provisions of Sections 34, 35, 58 and 59 as applicable to the document are complied with, the registering officer shall endorse thereon a certificate containing the word "registered" along with the number, and page of the book in which the document has been copied. The certificate shall be signed, sealed and dated by the registering officer.
- (b) The certificate of registration in respect of a document is *prima facie* an evidence that the document has been legally registered and raises a presumption that the registering officer proceeded in accordance with the law. (Section 60) (See Mulla (1998), pages 296, 297)

## **PROCEDURE AFTER REGISTRATION OF DOCUMENTS RELATING TO LAND**

- (1) On registering any non-testamentary document relating to immovable property the Registrar shall forward a memorandum of such document to each Sub-Registrar subordinate to himself in whose sub-district any part of the property is situate.
- (2) The Registrar shall also forward a copy of such document, together with a copy of map or plan (if any) mentioned in Section 21 to every Registrar in whose district any part of such property is situate.
- (3) Such Registrar, on receiving any such copy, shall file it in his Book No. 1 and shall also send a memorandum of the copy to the Sub-Registrar subordinate to him within whose sub-district any part of the property is situate.
- (4) Every Sub-Registrar receiving any memorandum under this Section shall file it in his Book No. 1. (Sections 64 to 65)

## **PROCEDURE AFTER REGISTRATION**

On any document being registered under Section 30(2), a copy of such document and of the endorsements and certificate thereon shall be forwarded to every Registrar within whose district any part of the property to which the instrument relates is situate, and the Registrar receiving such copy shall follow the procedure as prescribed in Sub-section (1) of Section 66.

## **REFUSAL TO REGISTER BY THE SUB-REGISTRAR**

Reasons for refusal to register to be recorded

- (1) Every Sub-Registrar refusing to register a document, except on the ground that the property to which it relates is not situate within his sub-district, shall make an order of refusal and record his reasons for such order in his Book No. 2 and endorse the words "Registration refused" on the document; and, on application made by any person executing or claiming under the document, shall without payment and unnecessary delay, give him a copy of the reasons so recorded.
- (2) No registering officer shall accept for registration a document so endorsed unless and until, under the provisions hereinafter contained, the document is directed to be registered. (Section 71)

Registration cannot be refused on the ground of undervaluation for stamp or any other extraneous reason. (Mulla (1998), page 308)

**Test your knowledge****Choose the correct answer**

Extension of time limit for registration can be authorized by:

- (a) Only Registrar
- (b) Registrar and Sub Registrar jointly
- (c) By Sub Registrar
- (d) None of the above



**Correct Answer: (a)**

**APPEAL TO REGISTRAR**

According to Section 72(1), an appeal shall lie against an order of a Sub-Registrar refusing to admit a document to registration (whether the registration of such document is compulsory or optional) to the Registrar to whom such Sub-Registrar is subordinate if presented to such Registrar within thirty days from the date of the order; and the Registrar may reverse or alter such order. This does not apply where the refusal is on the ground of denial of execution.

If the order of the Registrar directs the document to be registered and the document is duly presented for registration within thirty days after the making of such order, the Sub-Registrar shall obey the same, and thereupon shall, so far as may be practicable, follow the procedure prescribed in Sections 58, 59 and 60; and such registration shall take effect as if the document had been registered when it was first duly presented for registration. [Section 72(2)]

**APPLICATION TO REGISTRAR**

Refusal to register on the ground of denial of execution is governed by Section 73, under which the aggrieved party can make an "application" not appeal to the Registrar. (Section 73) (For denial of execution see Section 35)

**PROCEDURE BEFORE THE REGISTRAR**

In the case falling under Section 73 (refusal to register on the ground of denial of execution before the Sub-Registrar) and also where denial of registration is made before the Registrar himself, the Registrar shall inquire:

- (a) whether the document has been executed; and
- (b) whether the requirements of the law have been satisfied so as to entitle the document to registration. (Section 74)

**If a person denies execution, the Sub-Registrar must refuse registration leaving the parties to appeal under Section 73 (*Chhotey Lal v. Collector of Moradabad*, AIR 1922 PC 279). Ultimate remedy is a suit under Section 77 (*Ka Plinis Mysthong v. Ring Pyrbot*, AIR 1965 A.N. 42).**

**ORDER BY REGISTRAR TO REGISTER AND PROCEDURE THEREON**

If the Registrar finds that the document has been executed and that the said requirements have been complied with, he shall order the document to be registered (Section 75).

## INSTITUTION OF SUIT IN CASE OF ORDER OF REFUSAL BY REGISTRAR

Where the Registrar refuses to order the document to be registered any person claiming under such document, or his representative, assign or agent, may, within thirty days after the making of the order of refusal, institute in the Civil Court, within the local limits of whose original jurisdiction is situate the office in which the document is sought to be registered a suit for a decree directing the document to be registered in such office if it be duly presented for registration within thirty days after the passing of such decree. (Section 77)

### Test your knowledge

**State whether the following statement is “True” or “False”**

*Between two registered documents, the date of execution determines the priority.*

- *True*
- *False*

**Correct Answer: True**



## EXEMPTION OF CERTAIN DOCUMENTS EXECUTED BY OR IN FAVOUR OF GOVERNMENT

(1) Nothing contained in this Act in the Indian Registration Act, 1877 or in the Indian Registration Act, 1871 or in any Act thereby repealed, shall be deemed to require, or to have at any time required, the registration of any of the following documents or maps, namely:

- (a) documents issued, received or attested by any officer engaged in making a settlement or revision of settlement of land revenue and which form part of the records of such settlement; or
- (b) documents and maps issued, received or authenticated by any officer engaged on behalf of Government in making or revising the survey of any land which form part of the record of such survey; or
- (c) documents which, under any law for the time being in force are filed periodically in any revenue office by *patwaris* or other officers charged with the preparation of village records; or
- (d) *sanads, inam*, title deeds and other documents purporting to be an evidence, grants or assignments by Government of land or of any interest in land; or
- (e) *notices* given under section 74 or section 76 of the Bombay Land Revenue Code, 1879 of relinquishment of occupancy by occupants or of land by holders of such land.

(2) All such documents and maps shall for the purposes of Sections 48 and 49, be deemed to have been, and to be, registered in accordance with the provisions of this Act. (Section 90)

### LESSON ROUND-UP

- Registration of documents relating to immovable property is compulsory. Registration of will is optional. Some documents though related to immovable property are not required to be registered. These are given in Section 17(2) of the Act.
- Document should be submitted for registration within four months from date of execution. Decree or order of Court can be submitted within four months from the day it becomes final. If document is executed by several persons at different times, it may be presented for registration within four months from date of each execution. If a document is executed abroad by some of the parties, it can be presented for registration within four months after its arrival in India.

- If a person finds that a document has been filed for registration by a person who is not empowered to do so, he can present the document for re-registration within four months from the date he became aware of the fact that registration of document is invalid.
- Documents relating to immovable property should be registered in the office of Sub-Registrar of sub-district within which the whole or some portion of property is situated. Other documents can be registered in the office of Sub-Registrar. Where all persons executing the document desire it to be registered. Registrar can accept a document which is registrable with Sub-Registrar who is subordinate to him. Document should be presented for registration at the office of Registrar/Sub-Registrar. However, in special case, the officer may attend residence of any person to accept a document or will.
- All persons executing the document or their representatives, assign or agents holding power of attorney must appear before registering officer. They have to admit execution and sign the document in presence of Registrar, as required under Section 58(1)(a). Appearance may be simultaneous or at different times. If some of the persons are unable to appear within four months, further time upto additional four months can be given on payment of fine upto 10 times the proper registration fee.
- If the Registering Officer is satisfied about identity of persons and if they admit about execution of documents, and after registration fees are paid, the registering officer will register the document. He will make necessary entries in the Register maintained by him.
- After all formalities are complete, the Registering Officer will endorse the document with the word 'Registered', and sign the same. The endorsement will be copied in Register. After registration, the document will be returned to the person who presented the document.
- A document takes effect from its date of execution and not from date of registration. However, if the document states that it will be effective from a particular date, it will be effective from that date.
- Any non-testamentary document registered under the Act takes effect against any oral agreement relating to the property. The only exceptions are: (a) if possession of property (movable or immovable) is delivered on the basis of such oral agreement and such delivery of possession is valid transfer under any law (b) mortgage by deposit of title deeds takes effect against any mortgage deed subsequently executed and registered which relates to some property.

### SELF-TEST QUESTIONS

1. What is the object of the law of Registration?
2. Discuss the validity of the agreements in the following cases :
  - (a) A agrees to sell certain vehicles to *B*, the agreement is oral.
  - (b) A agrees to sell a garden to *B*, orally.
  - (c) A agrees to sell, to *B*, a health resort by a written agreement. The agreement is not registered.
3. A executes a sale deed of a garden in favour of *B*. The garden is situated in Udaipur. Can the sale deed be registered at Jaipur, which is the capital of Rajasthan?
4. A executes a mortgage of a house in favour of a bank, as a simple mortgage. It is not registered. Can the bank sue to enforce this mortgage?
5. A grants to *B* a mortgage by deposit of title-deeds. No document is executed or registered. Is the transaction valid?



EXECUTIVE PROGRAMME  
ECONOMIC AND COMMERCIAL LAWS

**EP-ECL**

**TEST PAPERS**

**A Guide to CS Students**

To enable the students in achieving their goal to become successful professionals, Institute has prepared a booklet 'A Guide to CS Students" providing the subject specific guidance on different papers and subjects contained in the ICSI curriculum. The booklet is available on ICSI website and students may download from <http://www.icsci.edu/Portals/0/AGUIDETOCSSTUDENTS.pdf>

**WARNING**

It is brought to the notice of all students that use of any malpractice in Examination is misconduct as provided in the explanation to Regulation 27 and accordingly the registration of such students is liable to be cancelled or terminated. The text of regulation 27 is reproduced below for information:

"27. Suspension and cancellation of examination results or registration

In the event of any misconduct by a registered student or a candidate enrolled for any examination conducted by the Institute, the Council or the Committee concerned may suo motu or on receipt of a complaint, if it is satisfied that, the misconduct is proved after such investigation as it may deem necessary and after giving such student or candidate an opportunity to state his case, suspend or debar the person from appearing in any one or more examinations, cancel his examination result, or studentship registration, or debar him from future registration as a student, as the case may be.

Explanation - Misconduct for the purpose of this regulation shall mean and include behaviour in a disorderly manner in relation to the Institute or in or near an Examination premises/centre, breach of any regulation, condition, guideline or direction laid down by the Institute, malpractices with regard to postal or oral tuition or resorting to or attempting to resort to unfair means in connection with the writing of any examination conducted by the Institute".

EXECUTIVE PROGRAMME  
**ECONOMIC AND COMMERCIAL LAWS**

**TEST PAPER 1**

*(This Test Paper is for recapitulate and practice for the students. Students need not to submit responses/answers to this test paper to the Institute.)*

Time Allowed: 3 hours

Maximum Marks: 100

Total number of questions: 6

NOTE: Answer ALL Questions

**PART A**  
**(Economic Laws)**

1. Write notes on the following:

- (a) Current Account Transactions
- (b) Foreign Source
- (c) Conditions conducive to cartelisation
- (d) Consumer under Consumer Protection Act, 1986
- (e) Doctrine of *Lis pendens*.

(5 marks each)

*Attempt all parts of either Q.No.2 or Q.No.2A*

- 2. (a) Explain the 'Assignment of a trade mark' and 'transmission of a trade mark' under the Trade Marks Act, 1999.
- (b) With reference to the relevant provisions of the Foreign Exchange Management Act, 1999 and the rules and regulations made thereunder, advise Rajiv, a person resident in India, who wishes to acquire foreign securities as qualification shares issued by a company incorporated outside India for holding the position of a director in the company.
- (c) Discuss the powers of the Central Government to prohibit receipt of foreign contribution under the Foreign Contribution (Regulation) Act, 2010.

(5 marks each)

*OR*

*(Alternate question to Q.No.2)*

- 2A. (a) State "Doctrine of Election" under Transfer of Property Act, 1882.
  - (b) State form and contents of an arbitral award.
  - (c) What are the modes of cancellation of adhesive stamps?
  - (d) Distinguish 'English mortgage' and 'mortgage by conditional sale'.
  - (e) State 'quasi contract'.
- (3 marks each)
- 3. (a) A school owned a swimming pool and offered swimming facilities to the public on payment of fees. The school conducted summer swimming training camps to train children in swimming and for this purpose had engaged a trainer/coach. Raghuraj had enrolled his son for learning how to swim. One day while swimming, the child died due to drowning. The school authorities maintained that the trainer/ coach was fully qualified for the job and challenged the complainant's claim for compensation in the consumer disputes redressal forum. Should the school authorities be held liable to pay compensation for 'deficiency in service'? Who is entitled to receive compensation? Give reasons.

- (b) A minor's contract is void ab initio, yet he enjoys special status under the Indian Contract Act, 1872. Explain.
- (c) State the salient features of the Special Economic Zones Act, 2005. (5 marks each)
4. (a) What are the factors that may be considered by Competition Commission of India for determining the 'Relevant Geographic Market' and 'Relevant Product Market'? Explain. (8 marks)
- (b) Certain acts do not constitute infringement of copyright under Copyright Act, 1957. Discuss. (7 marks)

**PART B**  
**(Commercial Laws)**

5. (a) State the provisions regarding Pre-packaged commodity under Legal Metrology Act, 2009.
- (b) State the Hazardous substance under Public Liability Insurance Act, 1991.
- (c) State the places where documents relating to immovable property may be presented for registration under the Registration Act, 1908.
- (d) What do you mean by the "day of acceptance" under Micro, Small and Medium Enterprises Development Act, 2006?
- (e) State the status of a society registered under Societies Registration Act, 1860 (3 marks each)

*Attempt all part of either Q. No. 6 or Q. No. 6A*

6. (a) Mention the powers of the central government to protect and improve the quality of environment under the Environment (Protection) Act, 1986.
- (b) What are the heads under which compensation or relief for damages may be claimed under the National Green Tribunal Act, 2010?
- (c) Discuss the powers and duties of Registrar of Societies. (5 marks each)

*OR*

*(Alternate question to Q. No. 6)*

- 6A. (a) Discuss the Doctrine of Cypres.
- (b) State the seizure and confiscation of essential commodities under the Essential Commodities Act, 1955.
- (c) List out the industries specified in the First Schedule of the Industries (Development and Regulation) Act, 1951 (5 marks each)

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## TEST PAPER 2

**(This Test Paper is for recapitulate and practice for the students. Students need not to submit responses/answers to this test paper to the Institute.)**

Time Allowed: 3 hours

Maximum Marks: 100

NOTE: Total number of questions: 6

Answer ALL Questions

### PART A (Economic Laws)

1. Write short notes on the following:
  - (a) Capital Account Transactions
  - (b) Foreign contribution
  - (c) Relevant Product Market
  - (d) Moral Rights of Author
  - (e) Flaws in Contract.

(5 marks each)

*Attempt all parts of either Q.No.2 or Q.No.2A*

2. (a) What do you mean by performer's right? Discuss exclusive right of performer under Copyright Act, 1957.
- (b) Discuss about Foreign Direct Investment in Multi Brand Retail Trading.
- (c) What is combination? Discuss thresholds for combinations under the Competition Act, 2002.

(5 marks each)

*OR*

*(Alternate question to Q.No.2)*

- 2A. (a) State the instruments which are chargeable with duty under the Indian Stamp Act, 1899.
- (b) State 'Actionable claim' under the Transfer of Property Act, 1882.
- (c) Mention the circumstances under which refund of stamp duty or penalty may be made by revenue authorities.
- (d) State 'Defect' in goods under the Consumer Protection Act, 1986.
- (e) State "Registered user" under the Trade Marks Act, 1999. (3 marks each)
3. (a) State the essential elements of a valid contract.
- (b) Distinguish between 'movable property' and 'immovable property'.
- (c) Mention the obligations of banking companies, financial institutions and intermediaries under the Prevention of Money Laundering Act, 2002. (5 marks each)
4. (a) What are the factors which the Competition Commission of India will take into consideration in determining whether an agreement has an appreciable adverse effect on competition? (8 marks)
- (b) Mention the cases that do not qualify to be called as inventions, within the meaning of the Patents Act, 1970? (7 marks)

### PART B (Commercial Laws)

5. (a) What do you mean by "substantial question relating to environment" under the National Green Tribunal Act, 2010.

- (b) Discuss briefly the takeover of the management of an industrial undertaking under Industries (Development and Regulation) Act, 1951.
- (c) Discuss briefly about Control of Noise Pollution under the Noise Pollution (Regulation and Control) Rules, 2000.
- (d) Describe the functions of the National Board for micro, small and medium enterprises under the Micro, Small and Medium Enterprises Development Act, 2006
- (e) Briefly explain Environmental Audit. (3 marks each)

*Attempt all part of either Q. No. 6 or Q. No. 6A*

- 6. (a) Mention the documents which are not required to be registered compulsorily under the Registration Act, 1908.
- (b) An enterprise which is engaged in hazardous or inherently dangerous activity and an industry which poses a potential threat to the health and safety of the persons and of those residing in the surrounding areas owes an absolute and non-delegatable duty to the community. Comment.
- (c) Discuss about the classification of Trusts. (5 marks each)

*OR*

*(Alternate question to Q. No. 6)*

- 6A. (a) Discuss briefly the memorandum of Micro, Small and Medium Enterprise.
  - (b) Discuss the powers of Central Government to control production, supply and distribution etc, of essential commodities under the Essential Commodities Act, 1955.
  - (c) What are the restrictions on the use of industrial plants under the Air(Prevention and Control of Pollution)Act, 1981? (5 marks each)
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