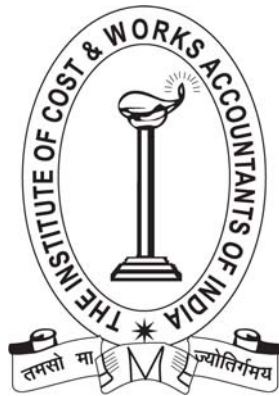


Commercial & Industrial Laws and Auditing

INTERMEDIATE : PAPER - 6

STUDY NOTES



**THE INSTITUTE OF
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Syllabus

Paper 6: Commercial & Industrial Laws and Auditing

(One Paper: 3 hours:100 marks)

OBJECTIVES

To give an exposure some of important commercial laws essential for an understanding of the legal implications of the modern business. Introduction to cover fundamental elements of the Legal System and the system of judicial precedent. The study to include essentials of establishing and performing simple contracts and the remedies available in the event of a breach and an introduction to company law.

To gain expert knowledge of the Principles and Practice of auditing and assurance and their application to different practical situations.

Learning Aims

The syllabus aim to test the student's ability to:

- Explain fundamental aspects of the organisation and operation of the Legal System;
- Identify and explain the essential elements of a simple contract, what is regarded as adequate performance of the simple contract, and the remedies available to the innocent party in the event of a breach;
- Explain the essential differences between sole traderships, partnerships and companies limited by shares;
- Explain the way in which companies are administered, financed and managed;
- Understanding the concepts of auditing, and auditing technique.
- To gain knowledge on procedure of auditing in different business environment.

Skill set required

Level B: Requiring the skill levels of knowledge, comprehension, application, and analysis.

CONTENTS

SECTION I: COMMERCIAL & INDUSTRIAL LAW	50%
1. Laws of Contracts	15%
2. Laws relating to Sale of Goods	10%
3. Industrial Laws	20%
4. Other Laws	5%

SECTION II : AUDITING**50%**

5. Auditing Basics	10%
6. Companies Act provisions relating to Audits	10%
7. Review and Audit of Internal Control Systems	15%
8. Information System Audit	10%
9. Introduction to Management Audit	5%

SECTION : I COMMERCIAL & INDUSTRIAL LAW**1. Laws of Contracts**

- Essential elements of a valid simple contract.
- Legal status of the various types of statements which may be made by negotiating parties. Enforceable offers and acceptances, and the application of the rules to standard form contracts and modern forms of communication.
- Meaning and importance of consideration.
- Principles for establishing that the parties intend their agreement to have contractual force.
- How a contract is affected by a misrepresentation.
- Conditions and warranties
- Manner in which law controls use of exclusion clauses and unfair terms in consumer and non-consumer transactions
- Level of performance sufficient to discharge contractual obligations
- Valid reasons for non-performance by way of agreement, breach by the other party and frustration

2. Laws relating to Sale of Goods

- Formation of Contract of sale
- Conditions and warranties
- Transfer of ownership and delivery of goods
- Unpaid seller and his rights

3. Industrial Laws

- Factories Act
- Industrial Dispute Act
- Workman Compensation Act
- Payment of Wages Act, Minimum Wages Act

- Provident Funds Act
- Payment of Bonus Act
- Payment of Gratuity Act
- Consumer Protection Act etc

4. Other Laws

- Limited Liability Partnership
- RTI Act
- Competition Commission Act
- Negotiable Instruments Act.

SECTION II: AUDITING

5. Auditing Basics

- Major influences of auditing; nature and scope of auditing; basic concepts of auditing; role of evidence in auditing; auditing techniques and practices – generally accepted auditing standards; the concept of materiality in auditing.
- Fixed assets, investments, inventories, debtors, loans and advances, cash and bank balances, debentures and creditors, provisions for taxation, proposed dividend and gratuity – other items in the balance sheet; verification of items in the profit and loss account; contingent liabilities; disclosure of accounting policies, practice; expenditure during the period of construction; adjustments for previous year – provisions of the Companies Act, 1956 regarding accounts.
- Statistical sampling in auditing. Use of ratios and percentages for comparison and analysis trends - inter-firm and intra-firm comparison.

6. Companies Act Provisions relating to Audits

- Auditors' appointment, remuneration, removal, rights of statutory auditors, duties of statutory auditors, joint auditors, branch audits.
- Report versus certificate, contents of the reports, qualifications in the report.
- Relevant provisions of the Companies Act, 1956 and the Income-tax Act, 1961.
- Interface between statutory auditor and internal auditor.
- Corporate Governance

7. Review and Audit of Internal Control Systems

- Nature and scope of internal auditing, financial versus operational audit; concepts of efficiency audit, propriety audit, voucher audit, compliance audit, pre and post audits.
- CARO
- Audit Report
- Internal auditing function
- Planning and process of internal audit
- Verification of evidence, detailed checking versus sampling plans, statistical sampling as used in internal auditing; flow chart techniques.
- Internal control, nature and scope, internal auditor and internal controls.
- Field work, collecting evidences, interviews; memoranda.
- Audit notes and working papers.
- Audit reports - techniques of effective reporting; follow up of audit report.
- Summary reports of top management.
- Communications in internal auditing - improving auditor-auditee relationship.
- Scope of Audit Committee
- Internal audit and investigation of fraud

8. Information System Audit.

9. Introduction to Management Audit.

Paper 6 : COMMERCIAL & INDUSTRIAL LAWS AND AUDITING

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Section - I

**COMMERCIAL
&
INDUSTRIAL LAWS**



Study Note – 1

INDIAN CONTRACT ACT, 1872

This study note includes

- Indian Contract Act, 1872-Concepts and Definitions
- Communication, Acceptance and Revocation of Proposals
- Contracts, Voidable Contracts and Void Agreements
- Free Consent
- Considerations
- Void Agreements
- Contingent Contracts
- The Performance of Contracts
- Time and Place for Performance
- Performance of Reciprocal Promises
- Appropriation of Payments
- Indemnity and Guarantee
- Bailment
- Bailment of Pledges
- Contracts of Agency

1.1 INDIAN CONTRACT ACT, 1872 - CONCEPTS AND DEFINITIONS

INTRODUCTION

The word CONTRACT is common to all of us and virtually no business transactions can take place without any contracts. The Indian Contract Act, 1872, deals with various types of contracts entered into by various people and defines the extremely important aspects of business transactions relating to contracts. In business dealings offers for sale are made and accepted, consideration is agreed, and conditions of sale are specified. Disputes arise when an offer or acceptance is violated, consideration is unpaid, and conditions of transactions are violated.

EXTENT AND COMMENCEMENT

The Indian Contract Act, 1872 extends to the whole of India except the State of Jammu and Kashmir; and it shall come into force on the first day of September, 1872.

ENACTMENTS REPEALED

The Indian Contract Act, 1872 does not affect nor does expressly repeal any provisions of any Statute, Act or Regulation and also does not expressly repeal any usage or custom of trade, nor any incident of any contract, not inconsistent with the provisions of this Act.

BASIC CONCEPTS

- (a) When one person signifies to another, his willingness to do or to 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;

- ### 1.1.1 Essential elements of a valid contract

-
- COMMERCIAL & INDUSTRIAL LAWS



The communication of proposals, the acceptance of proposals, and the revocation of proposals and acceptances, respectively, are deemed to be made by any act or omission of the party proposing, accepting or revoking, by which he intends to communicate such proposal, acceptance or revocation, or which has the effect of communicating it.

COMMUNICATION WHEN COMPLETE

The communication of a proposal is complete when it comes to the knowledge of the person to whom it is made.

THE COMMUNICATION OF AN ACCEPTANCE IS COMPLETE

As against the proposer, when it is put in a course of transmission to him, so as to be out of the power of the acceptor;

As against the acceptor, when it comes to the knowledge of the proposer.

THE COMMUNICATION OF A REVOCATION IS COMPLETE

As against the person who makes it, when it is put into a course of transmission to the person to whom it is made, so as to be out of the power of the person who makes it; as against the person to whom it is made, when it comes to his knowledge.

ILLUSTRATIONS

- (a) A proposes, by letter, to sell a house to B at a certain price.

The communication of the proposal is complete when B receives the letter.

- (b) B accepts A's proposal by a letter sent by post.

The communication of the acceptance is complete—as against A, when the letter is posted; as against B, when the letter is received by A.

- (c) A revokes his proposal by telegram.

The revocation is complete as against A when the telegram is despatched. It is complete as against B when B receives it.

B revokes his acceptance by telegram. B's revocation is complete as against B when the telegram is despatched, and as against A when it reaches him.

REVOCATION OF PROPOSALS AND ACCEPTANCES

A proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards.

An acceptance may be revoked at any time before the communication of the acceptance, is complete as against the acceptor, but not afterwards.

ILLUSTRATIONS

A proposes, by a letter sent by post, to sell his house to B.

B accepts the proposal by a letter sent by post.

A may revoke his proposal at any time before or at the moment when B posts his letter of acceptance, but not afterwards.

B may revoke his acceptance at any time before or at the moment when the letter communicating it reaches A, but not afterwards.

REVOCATION HOW MADE

A proposal is revoked—

- (1) By the communication of notice of revocation by the proposer to the other party;
- (2) By the lapse of the time prescribed in such proposal for its acceptance, or, if no time is so prescribed, by the lapse of a reasonable time, without communication of the acceptance;
- (3) By the failure of the acceptor to fulfill a condition precedent to acceptance; or
- (4) By the death or insanity of the proposer, if the fact of the death or insanity comes to the knowledge of the acceptor before acceptance.



FREE CONSENT [See 14]

Consent is said to be free when it is not caused by—

- (1) coercion, or
- (2) undue influence, or
- (3) fraud, or
- (4) misrepresentation, or
- (5) mistake, subject to provisions of sec 20, 21 and 22.

Consent is said to be so caused when it would not have been given but for the existence of such coercion, undue influence, fraud, misrepresentation or mistake.

(1) COERCION [See 15]

“Coercion” is the committing or threatening to commit, any act forbidden by the Indian Penal Code (45 of 1860), or the 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.

Explanation: It is immaterial whether the Indian Penal Code (45 of 1860) is or is not in force in the place where the coercion is employed.

Illustrations

A, on board an English ship on the high seas, causes B to enter into an agreement by an act amounting to criminal intimidation under the Indian Penal Code (45 of 1860).

A afterwards sues B for breach of contract at Calcutta.

A has employed coercion, although his act is not an offence by the law of England, and although section 506 of the Indian Penal Code (45 of 1860) was not in force at the time when, or at the place where the act was done.

(2) UNDUE INFLUENCE [See 16]

- (1) A contract is said to be induced 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.
- (2) In particular and without prejudice to the generality of the forgoing principle, 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; or
 - (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.
- (3) Where a person, who is in a position to dominate the will of another, enters into a contract with him, and the transaction appears, on the face of it or on the evidence adduced, to be unconscionable, the burden of proving that such contract was not induced by undue influence shall lie upon the person in a position to dominate the will of the other.

Nothing in this sub-section shall affect the provisions of section 111 of the Indian Evidence Act, 1872 (1 of 1872).

There is presumption of undue influence in the following relationships:

- (i) Parent and child
- (ii) Guardian and ward
- (iii) Doctor and patient
- (iv) Solicitor and client
- (v) Trustee and beneficiary
- (vi) Religious advisor and disciple
- (vii) Fiance and fiancée



There is however no presumption of undue influence in case of relationship of— (i) landlord and tenant (ii) debtor and creditor (iii) husband and wife. The wife has to be *pardanashin* for such presumption. In these relationships undue influence has to be proved.

Illustrations

- (a) 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 from B for a greater amount than the sum due in respect of the advance. A employs undue influence.
- (b) 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.
- (c) A, being in debt to B, the moneylender of his village, contracts a fresh loan on terms which appear to be unconscionable. It lies on B to prove that the contract was not induced by undue influence.
- (d) A applies to a banker for a loan at a time when there is stringency in the money market. The banker declines to make the loan except at an unusually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence.

(3) FRAUD [See 17]

“Fraud” means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent, with intent to deceive another party thereto or his agent, or to induce him to enter into the contract:—

- (1) The suggestion, as a fact, of that which is not true by one who does not believe it to be true;
- (2) The active concealment of a fact by one having knowledge or belief of the fact;
- (3) A promise made without any intention of performing it;
- (4) Any other act fitted to deceive;
- (5) Any such act or omission as the law specially declares to be fraudulent.

Explanation : Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech.

Illustrations

- (a) A sells, by auction, to B, a horse which A knows to be unsound. A says nothing to B about the horse's unsoundness. This is not fraud in A.
- (b) B says to A - “If you do not deny it, I shall assume that the horse is sound”. A says nothing. Here, A's silence is equivalent to speech.
- (c) A and B, being traders, enter upon a contract. A has private information of a change in prices which would affect B's willingness to proceed with the contract. A is not bound to inform B.

(4) MISREPRESENTATION [See 18]

“Misrepresentation” means and includes—

- (1) The positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;
- (2) Any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or any one claiming under him, by misleading another to his prejudice or to the prejudice of anyone claiming under him ;
- (3) Causing, however innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement.



(5) MISTAKE

Mistake means an erroneous belief about something.

Mistake can be -

- (a) Mistake of law, or
- (b) Mistake of fact.

(a) MISTAKE OF LAW

When a party enters into a contract, without the knowledge of law in the country, the contract is affected by such mistake but it is not void. A contract is not voidable because it was caused by a mistake as to any law in force in India. The reason here is that ignorance of law is not an excuse at all. However if a party is *induced* to enter into a contract by the mistake of law then such a contract is not valid.

Illustration

A and B make a contract grounded on the erroneous belief that a particular debt is barred by the Indian Law of Limitation; the contract is not voidable.

(b) MISTAKE OF FACT

Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void.

Explanation : An erroneous opinion as to the value of the thing which forms the subject-matter of the agreement is not to be deemed a mistake as to a matter of fact.

Illustrations

- (a) A agrees to sell to B a specific cargo of goods supposed to be on its way from England to Bombay. It turns out that, before the day of the bargain, the ship conveying the cargo had been cast away and the goods lost. Neither party was aware of the facts. The agreement is void.
- (b) A agrees to buy from B a certain horse. It turns out that the horse was dead at the time of the bargain, though neither party was aware of the fact. The agreement is void.
- (c) A, being entitled to an estate for the life of B, agrees to sell it to C. B was dead at the time of the agreement, but both parties were ignorant of the fact. The agreement is void.

CONTRACT CAUSED BY MISTAKE OF ONE PARTY AS TO MATTER OF FACT

A contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to a matter of fact.

VOIDABILITY OF AGREEMENTS WITHOUT FREE CONSENT

When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.

A party to a contract, whose consent was caused by fraud or misrepresentation, may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been, if the representations made had been true.

Exception : If such consent was caused by misrepresentation or by silence, fraudulent within the meaning of section 17, the contract, nevertheless, is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence.

Explanation: A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practiced, or to whom such misrepresentation was made, does not render a contract voidable.

Illustrations

- (a) A, intending to deceive B, falsely represents that five hundred mounds of indigo are made annually at A's factory, and thereby induces B to buy the factory. The contract is voidable at the option of B.



- (b) A, by a misrepresentation, leads B erroneously to believe that five hundred mounds of indigo are made annually at A's factory. B examines the accounts of the factory, which show that only four hundred mounds of indigo have been made. After this B buys the factory. The contract is not voidable on account of A's misrepresentation.
- (c) A fraudulently informs B that A's estate is free from encumbrance. B thereupon buys the estate. The estate is subject to a mortgage. B may either avoid the contract, or may insist on its being carried out and the mortgage-debt redeemed.
- (d) B, having discovered a vein of ore on the estate of A, adopts means to conceal, and does conceal, the existence of the ore from A. Through A's ignorance B is enabled to buy the estate at an undervalue. The contract is voidable at the option of A.
- (e) A is entitled to succeed to an estate at the death of B; B dies; C, having received intelligence of B's death, prevents the intelligence reaching A, and thus induces A to sell him his interest in the estate. The sale is voidable at the option of A.

POWER TO SET ASIDE CONTRACT INDUCED BY UNDUE INFLUENCE

When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused.

Any such contract may be set aside either absolutely, or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just.

Illustrations

- (a) A's son has forged B's name to a promissory note. B, under threat of prosecuting A's son, obtains a bond from A for the amount of the forged note. If B sues on this bond, the Court may set the bond aside.
- (b) A, a moneylender, advances Rs. 100 to B, an agriculturist, and, by undue influence, induces B to execute a bond for Rs. 200 with interest at 6 per cent per month. The Court may set the bond aside; ordering B to repay Rs. 100 with such interest as may seem just.

1.5 CONSIDERATION

INTRODUCTION

One of the essential elements of a contract is consideration. Consideration means something in return. For example, if A agrees to sale goods to B for a price of Rs. 20,000/-, the amount is the consideration for A for parting with the goods.

Sec.2(d) defines consideration as, 'When at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises to do or to abstain from doing, something, such act or abstinence or promise is called a consideration for the promise.'

An agreement without consideration is not enforceable and therefore is void.

In this chapter rules regarding consideration, exceptions to the rule of 'no consideration no contract' and other legal provisions are discussed.

Legal rules regarding consideration :

- (1) It must move at the desire of the promisor. Any act or abstinence at the desire of third party is not consideration.
- (2) It may move from the promisee or any other person. Consideration may be furnished even by a stranger under Indian Law.
- (3) It may be an act, abstinence or forbearance or a return promise.
- (4) It may be past, present or future — which the promisor is already not bound to do.
- (5) It must not be unlawful.

The consideration or object of an agreement is lawful, unless—



It is forbidden by law; or is of such a nature that, if permitted, it would defeat the provisions of any law; or is fraudulent; or involves or implies injury to the person or property of another; or the Court regards it as 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.

Example :

- (a) A agrees to sell his house to B for 10,000 rupees. Here B's promise to pay the sum of 10,000 rupees is the consideration for A's promise to sell the house, and A's promise to sell the house is the consideration for B's promise to pay the 10,000 rupees. These are lawful considerations.
- (b) A promises to pay B 10,000 rupees at the end of six months, if C who owes that sum to B, fails to pay it. B promises to grant time to C accordingly. Here the promise of each party is the consideration for the promise of the other party and they are lawful considerations.
- (c) A promises, for a certain sum paid to him by B, to make good to B the value of his ship if it is wrecked on a certain voyage. Here A's promise is the consideration for B's payment, and B's payment is the consideration for A's promise, and these are lawful considerations.
- (d) A promises to maintain B's child and B promises to pay A 1,000 rupees yearly for the purpose. Here the promise of each party is the consideration for the promise of the other party. They are lawful considerations.
- (e) A, B and C enter into an agreement for the division among them of gains acquired, or to be acquired, by them by fraud. The agreement is void, as its object is unlawful.
- (f) A promises to obtain for B an employment in the public service, and B promises to pay 1,000 rupees to A. The agreement is void, as the consideration for it is unlawful.
- (g) A, being agent for a landed proprietor, agrees for money, without the knowledge of his principal, to obtain for B a lease of land belonging to his principal. The agreement between A and B is void, as it implies a fraud by concealment by A, on his principal.
- (h) A promises B to drop a prosecution which he has instituted against B for robbery, and B promises to restore the value of the things taken. The agreement is void, as its object is unlawful.
- (i) A's estate is sold for arrears of revenue under the provisions of an act of the legislature, by which the defaulter is prohibited from purchasing the estate. B, upon an understanding with A, becomes the purchaser, and agrees to convey the estate to A upon receiving from him the price which B has paid. The agreement is void, as it renders the transaction, in effect, a purchase by the defaulter, and would so defeat the object of the law.
- (j) A, who is B's power of attorney holder, promises to exercise his influence, as such, with B in favour of C, and C promises to pay 1,000 rupees to A. The agreement is void, because it is immoral.
- (k) A agrees to let her daughter to hire to B for concubine. The agreement is void, because it is immoral, though the letting may not be punishable under the Indian Penal Code, (45 of 1860).

UN LAWFUL CONSIDERATION

The Agreements are void, if Considerations and objects unlawful in part.

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.

Example :

A promises to superintend, on behalf of B, a legal manufacture of indigo, and an illegal traffic in other articles. B promises to pay to A a salary of 10,000 rupees a year. The agreement is void, the object of A's promise and the consideration for B's promise, being in part unlawful.

NO CONSIDERATION

An agreement made without consideration is void, unless—

- (1) **Agreement without consideration void, unless it is in writing and registered.**—It is expressed in writing and registered under the law for the time being in force for the registration of documents, and is made on account of natural love and affection between parties standing in a near relation to each other.



- (2) **Or is a promise to compensate for something done.**— It is a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, or something which the promisor was legally compellable to do.
- (3) **Or is a promise to pay a debt barred by limitation law.**— It is a promise, made in writing and signed by the person to be charged therewith, or by his agent generally or specially authorized in that behalf, to pay wholly or in part a debt of which the creditor might have enforced payment but for the law for the limitation of suits.

In any of these cases, such an agreement is a contract.

Explanation 1: Nothing in this section shall affect the validity, as between the donor and donee, of any gift actually made.

Explanation 2: An agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate; but the inadequacy of the consideration may be taken into account by the Court in determining the question whether the consent of the promisor was freely given.

Example :

- (a) A promises, for no consideration, to give to B Rs. 1,000. This is a void agreement.
- (b) A, for natural love and affection, promises to give his son, B, Rs. 1,000. A puts his promise to B into writing and registers it. This is a contract.
- (c) A finds B's purse and gives it to him. B promises to give A Rs. 50. This is a contract.
- (d) A supports B's infant son. B promises to pay A's expenses in so doing. This is a contract.
- (e) A owes B Rs. 1,000, but the debt is barred by the Limitation Act. A signs a written promise to pay B Rs. 500 on account of the debt. This is a contract.
- (f) A agrees to sell a horse worth Rs. 1,000 for Rs. 10. A's consent to the agreement was freely given. The agreement is a contract notwithstanding the inadequacy of the consideration.
- (g) A agrees to sell a horse worth Rs. 1,000 for Rs. 10. A denies that his consent to the agreement was freely given. The inadequacy of the consideration is a fact which the court should take into account in considering whether or not A's consent was freely given.

1.6 VOID AGREEMENTS

INTRODUCTION

One of the essential elements of an enforceable agreement i.e. a contract is the lawfulness of the object. Behind any enforceable agreement there is an intention to create legal relationship which implies that there is some transaction. The object of such transaction should be lawful, else agreements shall not be enforceable by law.

AGREEMENT IN RESTRAINT OF MARRIAGE VOID

Every agreement in restraint of the marriage of any person, other than a minor, is void.

AGREEMENT IN RESTRAINT OF TRADE VOID

Every agreement by which anyone is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void.

Saving of agreement not to carry on business of which goodwill is sold.—

Exception 1.—One who sells the goodwill of a business may agree with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer, or any person deriving title to the goodwill from him, carries on a like business, therein :

Provided that such limits appear to the Court reasonable, regard being had to the nature of the business.

AGREEMENTS IN RESTRAINT OF LEGAL PROCEEDINGS VOID

Every agreement,—

- (a) by which any party thereto is restricted absolutely from enforcing his rights under or in respect of any



contract, by the usual legal proceedings in the ordinary tribunals, or which limits the time within which he may thus enforce his rights; or

- (b) which extinguishes the rights of any party thereto, or discharges any party thereto from any liability, under or in respect of any contract on the expiry of a specified period so as to restrict any party from enforcing his rights, is void to that *extent*.

Savings of contract to refer to arbitration dispute that may arise—

Exception 1.—This section shall not render illegal a contract, by which two or more persons agree that any dispute which may arise between them in respect of any subject or class of subjects shall be referred to arbitration, and that only the amount awarded in such arbitration shall be recoverable in respect of the dispute so referred.

Suits barred by such contracts.—When such a contract has been made, a suit may be brought for its specific performance, and if a suit, other than for such specific performance, or for the recovery of the amount so awarded, is brought by one party to such contract against any other such party, in respect of any subject which they have so agreed to refer, the existence of such contract shall be a bar to the suit.

Saving of contract to refer questions that have already arisen.—Exception 2.—Nor shall this section render illegal any contract in writing, by which two or more persons agree to refer to arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration.

AGREEMENTS VOID FOR UNCERTAINTY

Agreements, the meaning of which is not certain, or capable of being made certain, are void.

Example :

- (a) A agrees to sell to B “a hundred tons of oil”. There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty.
- (b) A agrees to sell to B one hundred tons of oil of a specified description, known as an article of commerce. There is no uncertainty here to make the agreement void.
- (c) A, who is a dealer in coconut oil only, agrees to sell to B “one hundred tons of oil”. The nature of A’s trade affords an indication of the meaning of the words, and A has entered into a contract for the sale of one hundred tons of coconut oil.
- (d) A agrees to sell to B “all the grain in my granary at Ramnagar”; There is no uncertainty here to make the agreement void.
- (e) A agrees to sell to B “one thousand maunds of rice at a price to be fixed by C”. As the price is capable of being made certain, there is no uncertainty here to make the agreement void.
- (f) A agrees to sell to B “my white horse for rupees five hundred or rupees one thousand”. There is nothing to show which of the two prices was to be given. The agreement is void.

AGREEMENTS BY WAY OF WAGER ARE VOID

Agreements by way of wager are void; and no suit shall be brought for recovering anything alleged to be won on any wager, or entrusted to a person to abide by the result of any game or other uncertain event on which any wager is made.

Exception in favour of certain prizes for horse-racing.—This section shall not be deemed to render unlawful a subscription, or contribution, or agreement to subscribe or contribute, made or entered into for or toward any plate, prize or sum of money, of the value or amount of five hundred rupees or upwards, to be awarded to the winner or winners of any horse-race.

Section 294A of the Indian Penal Code not affected.—Nothing in this section shall be deemed to legalize any transaction connected with horse-racing, to which the provisions of section 294A of the Indian Penal Code, (45 of 1860) apply.



1.7 CONTINGENT CONTRACTS

INTRODUCTION

There are some contracts wherein there is no element of uncertainty in their performance. In other words there performance is not dependent upon a particular event. Such contracts are known as 'absolute contracts'.

CONTINGENT CONTRACT

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.

Illustration

A contracts to pay B Rs. 10,000 if B's house is burnt. This is a contingent contract.

ENFORCEMENT OF CONTRACTS CONTINGENT ON AN EVENT HAPPENING

Contingent contracts to do or not to do anything if an uncertain future event happens cannot be enforced by law unless and until that event has happened.

If the event becomes impossible, such contracts become void.

Illustrations

- (a) A makes a contract with B to buy B's horse if A survives C. This contract cannot be enforced by law unless and until C dies in A's lifetime.
- (b) A makes a contract with B to sell a horse to B at a specified price, if C, to whom the horse has been offered, refuses to buy him. The contract cannot be enforced by law unless and until C refuses to buy the horse.
- (c) A contracts to pay B a sum of money when B marries C. C dies without being married to B. The contract becomes void.

ENFORCEMENT OF CONTRACTS CONTINGENT ON AN EVENT NOT HAPPENING

Contingent contracts to do or not to do anything if an uncertain future event does not happen can be enforced when the happening of that event becomes impossible, and not before.

Illustrations

A agrees to pay B a sum of money if a certain ship does not return. This ship is sunk. The contract can be enforced when the ship sinks.

WHEN EVENT ON WHICH CONTRACT IS CONTINGENT TO BE DEEMED IMPOSSIBLE, IF IT IS THE FUTURE CONDUCT OF A LIVING PERSON

If the future event on which a contract is contingent is the way in which 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.

Illustrations

A agrees to pay B a sum of money 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 that C may afterwards marry B.

WHEN CONTRACTS BECOME VOID WHICH ARE CONTINGENT ON HAPPENING OF SPECIFIED EVENT WITHIN FIXED TIME

Contingent contracts to do or not to do anything if a specified uncertain event happens within a fixed time become void if, at the expiration of the time fixed, such event has not happened, or if, before the time fixed, such event becomes impossible.



When contracts may be enforced which are contingent on specified event not happening within fixed time.—

Contingent contracts to do or not to do anything if a specified uncertain event does not happen 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.

Illustrations

- (a) 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.
- (b) A promises to pay B a sum of money if a certain ship does not return within a year. The contract may be enforced if the ship does not return within the year, or is burnt within the year.

AGREEMENTS CONTINGENT ON IMPOSSIBLE EVENTS VOID

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 to the parties to the agreement at the time when it is made.

Illustrations

- (a) A agrees to pay B 1,000 rupees if two-straight lines should enclose a space. The agreement is void.
- (b) A agrees to pay B 1,000 rupees if B will marry A's daughter C. C was dead at the time of the agreement. The agreement is void.

1.8 THE PERFORMANCE OF CONTRACTS

INTRODUCTION

Every Contract creates certain obligation on each of the parties involved in it. When both the parties to the Contract fulfill their obligations towards each other, the contract is said to be performed.

OBLIGATION OF PARTIES TO CONTRACTS

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 provisions of this Act, or of any other law.

Promises bind the representatives of the promisor in case of the death of such promisor before performance, unless a contrary intention appears from the contract.

Illustrations

- (a) A promises to deliver goods to B on a certain day on payment of Rs. 1,000. A dies before that day. A's representatives are bound to deliver the goods to B, and B is bound to pay Rs. 1,000 to A's representatives.
- (b) A promises to paint a picture for B by a certain day, at a certain price. A dies before the day. The contract cannot be enforced either by A's representatives or by B.

EFFECT OF REFUSAL TO ACCEPT OFFER OF PERFORMANCE

Where a promisor has made an offer of performance to the promisee, and the offer has not been accepted, the promisor is not responsible for non-performance, nor does he thereby lose his rights under the contract.

Every such offer must fulfill the following conditions :—

- (1) it must be unconditional
- (2) it must be made at a proper time and place, and under such circumstances that the person to whom it is made may have a reasonable opportunity of ascertaining that the person by whom it is made is able and willing there and then to do the whole of what he is bound by his promise to do:
- (3) if the offer is an offer to deliver anything to the promisee, 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.

An offer to one of several joint promisees has the same legal consequences as an offer to all of them.

**Illustrations**

A contracts to deliver to B at his warehouse, on the first March, 1873, 100 bales of cotton of a particular quality. In order to make an offer of a performance with the effect stated in this section, A must bring the cotton to B's warehouse, on the appointed day, under such circumstances that B may have a reasonable opportunity of satisfying himself that the thing offered is cotton of the quality contracted for, and that there are 100 bales.

EFFECT OF REFUSAL OF PARTY TO PERFORM PROMISE WHOLLY

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 has signified, by words or conduct, his acquiescence in its continuance.

Illustrations

- (a) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night A willfully absents herself from the theatre. B is at liberty to put an end to the contract.
- (b) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B engages to pay her at the rate of 100 rupees for each night. On the sixth night A willfully absents herself. With the assent of B, A sings on the seventh night. B has signified his acquiescence in the continuance of the contract, and cannot now put an end to it but is entitled to compensation for the damage sustained by him through A's failure to sing on the sixth night.

PERSON BY WHOM PROMISE IS TO BE PERFORMED

If it appears from the nature of the case that it was the intention of the parties to any contract that any promise contained in it should be performed by the promisor himself, such promise must be performed by the promisor. In other cases, the promisor or his representatives may employ a competent person to perform it.

Illustrations

- (a) A promises to pay B a sum of money. A may perform this promise, either by personally paying the money to B or by causing it to be paid to B by another; and, if A dies before the time appointed for payment, his representatives must perform the promise, or employ some proper person to do so.
- (b) A promises to paint a picture for B: A must perform this promise personally.

EFFECT OF ACCEPTING PERFORMANCE FROM THIRD PERSON

When a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

DEVOLUTION OF JOINT LIABILITIES

When two or more persons have made a joint promise then, unless a contrary intention appears by the contract, all such persons, during their joint lives, and after the death of any of them, his representative jointly with the survivor, or survivors, and after the death of the last survivor, the representatives of all jointly, must fulfill the promise.

ANY ONE OF JOINT PROMISORS MAY BE COMPELLED TO PERFORM

When two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any one or more of such joint promisors to perform the whole of the promise.

Each promisor may compel contribution.—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.

Sharing of loss by default in contribution.—If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal shares.



Explanation : Nothing in this section shall prevent a surety from recovering from his principal, payments made by the surety on behalf of the principal, or entitle the principal to recover anything from the surety on account of payments made by the principal.

Illustrations

- (a) A, B and C jointly promise to pay D 3,000 rupees. D may compel either A or B or C to pay him 3,000 rupees.
- (b) A, B and C jointly promise to pay D the sum of 3,000 rupees. C is compelled to pay the whole. A is insolvent, but his assets are sufficient to pay one-half of his debts, C is entitled to receive 500 rupees from A's estate, and 2,250 rupees from B.
- (c) A, B and C are under a joint promise to pay D 3,000 rupees. C is unable to pay anything, and A is compelled to pay the whole. A is entitled to receive 1,500 rupees from B.
- (d) A, B and C are under a joint promise to pay D 3,000 rupees, A and B being only sureties for C. C fails to pay. A and B are compelled to pay the whole sum. They are entitled to recover it from C.

EFFECT OF RELEASE OF ONE JOINT PROMISOR

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 or joint promisors; neither does it free the joint promisor so released from responsibility to the other joint promisor or joint promisors.

DEVOLUTION OF JOINT RIGHTS

When a person has made a promise to two or more persons jointly, then, unless a contrary intention appears from the contract, the right to claim performance rests, as between him and them, with them during their joint lives, and, after the death of any of them, with the representative of such deceased person jointly with the survivor or survivors, and, after the death of the last survivor, with the representatives of all jointly.

Illustration

A, in consideration of 5,000 rupees, lent to him by B and C, promises B and C jointly to repay them that sum with interest on a day specified. B dies. The right to claim performance rests with B's representative jointly with C during C's life, and after the death of C with the representatives of B and C jointly.

1.9 TIME AND PLACE FOR PERFORMANCE

TIME FOR PERFORMANCE OF PROMISE, WHERE NO APPLICATION IS TO BE MADE AND NO TIME IS SPECIFIED

Where, by the contract, a promisor is to perform his promise without application by the promisee, and no time for performance is specified, the engagement must be performed within a reasonable time.

Explanation: The question "What is a reasonable time" is, in each particular case, a question of fact.

TIME AND PLACE FOR PERFORMANCE OF PROMISE, WHERE TIME IS SPECIFIED AND NO APPLICATION TO BE MADE

When a promise is to be performed on a certain day, and the promisor has undertaken to perform it without application by the promisee, the promisor may perform it at any time during the usual hours of business on such day and at the place at which the promise ought to be performed.

Illustration

A promises to deliver goods at B's warehouse on the 1st January. On that day A brings the goods to B's warehouse, but after the usual hour for closing it, and they are not received. A has not performed his promise.

**APPLICATION FOR PERFORMANCE ON CERTAIN DAY TO BE AT PROPER TIME AND PLACE**

When a promise is to be performed on a certain day, and the promisor has not undertaken to perform it without application by the promisee, it is the duty of the promisee to apply for performance at a proper place and within the usual hours of business.

Explanation : The question “What is a proper time and place” is, in each particular case, a question of fact.

PLACE FOR PERFORMANCE OF PROMISE, WHERE NO APPLICATION TO BE MADE AND NO PLACE FIXED FOR PERFORMANCE.

When a promise is to be performed without application by the promisee, and no place is fixed for the performance of it, it is the duty of the promisor to apply to the promisee to appoint a reasonable place for the performance of the promise, and to perform it at such place.

Illustration

A undertakes to deliver a thousand maunds of jute to B on a fixed day. A must apply to B to appoint a reasonable place for the purpose of receiving it, and must deliver it to him at such place.

PERFORMANCE IN MANNER OR AT TIME PRESCRIBED OR SANCTIONED BY PROMISEE

The performance of any promise may be made in any manner, or at any time which the promisee prescribes or sanctions.

Illustrations

- (a) B owes A 2,000 rupees. A desires B to pay the amount to A's account with C, a banker. B, who also banks with C, orders the amount to be transferred from his account to A's credit, and this is done by C. Afterwards, and before A knows of the transfer, C fails. There has been a good payment by B.
- (b) A and B are mutually indebted. A and B settle an account by setting off one item against another, and B pays A the balance found to be due from him upon such settlement. This amounts to a payment by A and B respectively of the sums which they owed to each other.
- (c) A owes B 2,000 rupees. B accepts some of A's goods in deduction of the debt. The delivery of the goods operates as a part payment.
- (d) A desires B, who owes him Rs. 100, to send him a note for Rs. 100 by post. The debt is discharged as soon as B puts into the post a letter containing the note duly addressed to A.

1.10 PERFORMANCE OF RECIPROCAL PROMISES**PROMISOR NOT BOUND TO PERFORM UNLESS RECIPROCAL PROMISEE READY AND WILLING TO PERFORM**

When a contract consists of reciprocal promises to be simultaneously performed, no promisor need perform his promise unless the promisee is ready and willing to perform his reciprocal promise.

Illustrations

- (a) A and B contract that A shall deliver goods to B to be paid for by B on delivery.
A need not deliver the goods, unless B is ready and willing to pay for the goods on delivery.
B need not pay for the goods, unless A is ready and willing to deliver them on payment.
- (b) A and B contract that A shall deliver goods to B at a price to be paid by installments, the first installment to be paid on delivery.
A need not deliver, unless B is ready and willing to pay the first installment on delivery.
B need not pay the first installment, unless A is ready and willing to deliver the goods on payment of the first installment.



ORDER OF PERFORMANCE OF RECIPROCAL PROMISES

Where the order in which reciprocal promises are to be performed is expressly fixed by the contract, they shall be performed in that order; and,

where the order is not expressly fixed by the contract, they shall be performed in that order which the nature of the transaction requires.

Illustrations

- (a) A and B contract that A shall build a house for B at a fixed price. A's promise to build the house must be performed before B's promise to pay for it.
- (b) A and B contract that A shall make over his stock-in-trade to B at a fixed price, and B promises to give security for the payment of the money. A's promise need not be performed until the security is given, for the nature of the transaction requires that A should have security before he delivers up his stock.

LIABILITY OF PARTY PREVENTING EVENT ON WHICH THE CONTRACT IS TO TAKE EFFECT

When a contract contains reciprocal promises, and one party to the contract prevents the other from performing his promise, the contract becomes voidable at the option of the party so prevented; and he is entitled to compensation from the other party for any loss which he may sustain in consequence of the non-performance of the contract.

Illustration

A and B contract that B shall execute certain work for A for a thousand rupees. B is ready and willing to execute the work accordingly, but A prevents him from doing so. The contract is voidable at the option of B; and, if he elects to rescind it, he is entitled to recover from A compensation for any loss which he has incurred by its non-performance.

EFFECT OF DEFAULT AS TO THAT PROMISE WHICH SHOULD BE FIRST PERFORMED, IN CONTRACT CONSISTING OF RECIPROCAL PROMISES.

When a contract consists of reciprocal promises, such that one of them cannot be performed, or that its performance cannot be claimed till the other has been performed, and the promiser of the promise last mentioned fails to perform it, such promisor cannot claim the performance of the reciprocal promise, and must make compensation to the other party to the contract for any loss which such other party may sustain by the non-performance of the contract.

Illustrations

- (a) A hires B's ship to take in and convey, from Calcutta to the Mauritius, a cargo to be provided by A, B receiving a certain freight for its conveyance. A does not provide any cargo for the ship. A cannot claim the performance of B's promise, and must make compensation to B for the loss which B sustains by the non-performance of the contract.
- (b) A contracts with B to execute certain builder's work for a fixed price, B supplying the scaffolding and timber necessary for the work. B refuses to furnish scaffolding or timber, and the work cannot be executed. A need not execute the work, and B is bound to make compensation to A for any loss caused to him by the non-performance of the contract.
- (c) A contracts with B to deliver to him, at a specified price, certain merchandise on board a ship which cannot arrive for a month, and B engages to pay for the merchandise within a week from the date of the contract. B does not pay within the week. A's promise to deliver need not be performed, and B must make compensation.
- (d) A promises B to sell him one hundred bales of merchandise, to be delivered next day, and B promises A to pay for them within a month. A does not deliver according to his promise. B's promise to pay need not be performed and A must make compensation.

**TIME IS ESSENCE OF THE CONTRACT**

When a party to a contract promises to do a certain thing at or before a specified time, or certain things at or before specified times, and fails to do any such thing at or before the specified time, the contract, or so much of it as has not been performed, becomes voidable at the option of the promisee, if the intention of the parties was that time should be of the essence of the contract.

Effect of such failure when time is not essential—If it was not the intention of the parties that time should be of the essence of the contract, the contract does not become voidable by the failure to do such thing at or before the specified time; but the promisee is entitled to compensation from the promisor for any loss occasioned to him by such failure.

Effect of acceptance of performance at time other than that agreed upon.—If, in case of a contract voidable on account of the promisor's failure to perform his promise at the time agreed, the promisee accepts performance of such promise at any time other than that agreed, the promisee cannot claim compensation for any loss occasioned by the non-performance of the promise at the time agreed, unless, at the time of such acceptance, he gives notice to the promisor of his intention to do so.

AGREEMENT TO DO IMPOSSIBLE ACT

An agreement to do an act impossible in itself is void.

Contract to do act afterwards becoming impossible or unlawful.—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.

COMPENSATION FOR LOSS THROUGH NON-PERFORMANCE OF ACT KNOWN TO BE IMPOSSIBLE OR UNLAWFUL

Where one person has promised to do something which he knew, or, with reasonable diligence, might have known, and which the promisee did not know to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise.

Illustrations

- (a) A agrees with B to discover treasure by magic. The agreement is void.
- (b) A and B contract to marry each other. Before the time fixed for the marriage, A goes mad. The contract becomes void.
- (c) A contracts to marry B, being already married to C, and being forbidden by the law to which he is subject to practise polygamy. A must make compensation to B for the loss caused to her by the non-performance of his promise.
- (d) A contracts to take in cargo for B at a foreign port. A's Government afterwards declares war against the country in which the port is situated. The contract becomes void when war is declared,
- (e) A contracts to act at a theatre for six months in consideration of a sum paid in advance by B. On several occasions A is too ill to act. The contract to act on those occasions becomes void.

RECIPROCAL PROMISES TO DO THINGS LEGAL, AND ALSO OTHER THINGS ILLEGAL

Where persons reciprocally promise, firstly, to do certain things which are legal, and, secondly, under-specified circumstances, to do certain other things which are illegal, the first set of promises is a contract, but the second is a void agreement.

Illustration

A and B agree that A shall sell B a house for 10,000 rupees, but that, if B uses it as a gambling house, he shall pay A 50,000 rupees for it.

The first set of reciprocal promises, namely, to sell the house and to pay 10,000 rupees for it, is a contract.

The second set is for an unlawful object, namely, that B may use the house as a gambling house, and is a void agreement.



ALTERNATIVE PROMISE, ONE BRANCH BEING ILLEGAL

In the case of an alternative promise, one branch of which is legal and the other illegal, the legal branch alone can be enforced.

Illustration

A and B agree that A shall pay B 1,000 rupees, for which B shall afterwards deliver to A either rice or smuggled opium.

This is a valid contract to deliver rice, and a void agreement as to the opium.

1.11 APPROPRIATION OF PAYMENTS

APPLICATION OF PAYMENT WHERE DEBT TO BE DISCHARGED IS INDICATED

Where a debtor, owing several distinct debts to one person, makes a payment to him, either with express intimation, or under circumstances implying that the payment is to be applied to the discharge of some particular debt, the payment, if accepted, must be applied accordingly.

Illustrations

- (a) A owes B, among other debts, 1,000 rupees upon a promissory note which falls due on the first June. He owes B no other debt of that amount. On the first June A pays to B 1,000 rupees. The payment is to be applied to the discharge of the promissory note.
- (b) A owes to B, among other debts, the sum of 567 rupees. B writes to A and demands payment of this sum. A sends to B 567 rupees. This payment is to be applied to the discharge of the debt of which B had demanded payment.

APPLICATION OF PAYMENT WHERE DEBT TO BE DISCHARGED IS NOT INDICATED

Where the debtor has omitted to intimate and there are no other circumstances indicating to which debt the payment is to be applied, the creditor may apply it at his discretion to any lawful debt actually due and payable to him from the debtor, whether its recovery is or is not barred by the law in force for the time being as to the limitation of suits.

APPLICATION OF PAYMENT WHERE NEITHER PARTY APPROPRIATES

Where neither party makes any appropriation the payment shall be applied in discharge of the debts in order of time, whether they are or are not barred by the law in force for the time being as to the limitation of suits. If the debts are of equal standing, the payment shall be applied in discharge of each proportionately.

CONTRACTS WHICH NEED NOT BE PERFORMED EFFECT OF NOVATION, RESCISSION AND ALTERATION OF CONTRACT

If the parties to a contract agree to substitute a new contract for it, or to rescind or alter it, the original contract need not be performed.

Illustrations

- (a) A owes money to B under a contract. It is agreed between A, B and C that B shall thenceforth accept C as his debtor, instead of A. The old debt of A to B is at an end, a new debt from C to B has been contracted.
- (b) A owes B 10,000 rupees. A enters into an agreement with B, and gives B a mortgage of his (A's) estate for 5,000 rupees in place of the debt of 10,000 rupees. This is a new contract and extinguishes the old.
- (c) A owes B 1,000 rupees under a contract, B owes C 1,000 rupees. B orders A to credit C with 1,000 rupees in his books, but C does not assent to the arrangement. B still owes C 1,000 rupees, and no new contract has been entered into.

PROMISEE MAY DISPENSE WITH OR REMIT PERFORMANCE OF PROMISE

Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit.

**Illustrations**

- (a) A promises to paint a picture for B. B afterwards forbids him to do so A is no longer bound to perform the promise.
- (b) A owes B 5,000 rupees. A pays to B, and B accepts in satisfaction of the whole debt, 2,000 rupees paid at the time and place at which the 5,000 rupees were payable. The whole debt is discharged.
- (c) A owes B 5,000 rupees. C pays to B 1,000 rupees, and B accepts them, in satisfaction of his claim on A. This payment is a discharge of the whole claim.
- (d) A owes B, under a contract, a sum of money, the amount of which has not been ascertained. A without ascertaining the amount gives to B, and B, in satisfaction thereof, accepts the sum of 2,000 rupees. This is a discharge of the whole debt, whatever may be its amount.
- (e) A owes B 2,000 rupees, and is also indebted to other creditors. A makes an arrangement with his creditors, including B, to pay them, a composition of eight annas in the rupee upon their respective demands. Payment to B of 1,000 rupees is a discharge of B's demand.

CONSEQUENCES OF RESCISSION OF VOIDABLE CONTRACT

Where a person at whose option a contract is voidable rescinds it, the other party thereto need not perform any promise therein contained in which he is 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.

OBLIGATION OF PERSON WHO HAS RECEIVED ADVANTAGE UNDER VOID AGREEMENT OR CONTRACT THAT BECOMES VOID

When an agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it, to the person from whom he received it.

Illustrations

- (a) A pays B 1,000 rupees in consideration of B's promising to marry C, A's daughter. C is dead at the time of the promise. The agreement is void, but B must repay A the 1,000 rupees.
- (b) A contracts with B to deliver to him 250 maunds of rice before the 1st of May. A delivers 130 maunds only before that day, and none after. B retains the 130 maunds after the first day of May. He is bound to pay A for them.
- (c) A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her a hundred rupees for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B must pay A for the five nights on which she had sung.
- (d) A contracts to sing for B at a concert for 1,000 rupees, which are paid in advance. A is too ill to sing. A is not bound to make compensation to B for the loss of the profits which B would have made if A had been able to sing, but must refund to B the 1,000 rupees paid in advance.

MODE OF COMMUNICATING OR REVOKING RESCISSION OF VOIDABLE CONTRACT

The rescission of a voidable contract may be communicated or revoked in the same manner, and subject to the same rules, as apply to the communication or revocation of a proposal.

EFFECT OF NEGLIGENCE OF PROMISEE TO AFFORD PROMISOR REASONABLE FACILITIES FOR PERFORMANCE

If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any non-performance caused thereby.

Illustration

A contracts with B to repair B's house.



B neglects or refuses to point out to A the places in which his house requires repair.
A is excused for the non-performance of the contract if it is caused by such neglect or refusal.

CLAIM FOR NECESSARIES SUPPLIED TO PERSON INCAPABLE OF CONTRACTING, OR ON HIS ACCOUNT

If a person, incapable of entering into a contract, or anyone whom he is legally bound to support, is supplied by another person with necessities suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

Illustrations

- (a) A supplies B, a lunatic, with necessities suitable to his condition in life. A is entitled to be reimbursed from B's property.
- (b) A supplies the wife and children of B, a lunatic, with necessities suitable to their condition in life. A is entitled to be reimbursed from B's property.

REIMBURSEMENT OF PERSON PAYING MONEY DUE BY ANOTHER IN PAYMENT OF WHICH HE IS INTERESTED

A person who is interested in the payment of money which another is bound by law to pay, and who therefore pays it, is entitled to be reimbursed by the other.

Illustration

B holds land in Bengal, on a lease granted by A, the zamindar. The revenue payable by A to the Government being in arrear, his land is advertised for sale by the Government. Under the revenue law, the consequence of a such sale will be the annulment of B's lease. B, to prevent the sale and the consequent annulment of his own lease, pays to the Government the sum due from A. A is bound to make good to B the amount so paid.

OBLIGATION OF PERSON ENJOYING BENEFIT OF NON-GRATUITOUS ACT

Where a person lawfully does anything for another person/or delivers anything to him, not intending to do so gratuitously, and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered.

Illustrations

- (a) A, a tradesman, leaves goods at B's house by mistake, B treats the goods as his own. He is bound to pay A for them.
- (b) A saves B's property from fire. A is not entitled to compensation from-B, if the circumstances show that he intended to act gratuitously.

FINDER OF GOODS

A person who finds goods belonging to another, and takes them into his custody, is subject to the same responsibility as a bailee besides the responsibility of exercising reasonable efforts in finding the real owner.

However, a finder is also bestowed with certain rights as follows:

- (i) Right to retain the goods until the true owner compensates him for the money spent in preserving the goods and finding the owner. The finder, however, cannot sue for compensation. Where the owner has declared specific reward, the finder can sue him for the same.
- (ii) Right to sell-If the owner cannot be found after due search, or he refuses to pay lawful charges of the finder, the finder may sell the goods if-
 - (a) the goods are of perishable nature;
 - (b) lawful charges of the finder amounts to $\frac{2}{3}$ rd of the value of goods.

**LIABILITY OF PERSON TO WHOM MONEY IS PAID, OR THING DELIVERED BY MISTAKE OR UNDER COERCION**

A person to whom money has been paid, or anything delivered, by mistake or under coercion, must repay or return it.

Illustrations

- (a) A and B jointly owe 100 rupees to C. A alone pays the amount to C, and B, not knowing this fact, pays 100 rupees over again to C. C is bound to repay the amount to B.
- (b) A railway company refuses to deliver up certain goods to the consignee, except upon the payment of an illegal charge for carriage. The consignee pays the sum charged in order to obtain the goods. He is entitled to recover so much of the charge as was illegally excessive.

DISCHARGE OF CONTRACT

Discharge of Contract implies termination of contractual relationship among parties. A contract is discharged means it ceases to operate and rights and obligation under it comes to an end. A contract may be discharged by-

- (i) performance,
- (ii) mutual consent,
- (iii) subsequent impossibility of performance,
- (iv) lapse of time,
- (v) operation of law,
- (vi) breach of contract.

1. Discharge by performance is the most usual form of discharge of a contract. A contract is said to be performed when the parties fulfill their respective obligations.
2. A contract may be discharged by a further agreement among parties which may be expressed or implied.
3. A contract to perform an impossible act is void *ab initio*. A contract is discharged if subsequent performance becomes impossible due to factors beyond the control of the parties. Supervening impossibility occurs:
 - (a) When subject matter of contract is destroyed.
 - (b) When state of things which form basis of contract changes.
 - (c) When performance depends on personal skill, incapacity of that party renders the contract discharged.
 - (d) Change of law may render the performance impossible.
 - (e) Out break of war may make a party alien enemy. Contract with alien enemy is unlawful and such contracts are suspended during duration of war.

It should however be noted that 'impossibility of performance' as a rule cannot be an excuse for non-performance unless performance becomes absolutely impossible.

4. As per Law of Limitation, a contract should be performed within a specified time period, called period of limitation. If not performed within 'period of limitation' and no action is taken by the promisee, the contract is terminated.
5. A contract may be discharged due to operation of law by death of a party, merger, insolvency of a party, unauthorized alteration in terms of contract, rights and liabilities getting vested in the same person.
6. If a party to a contract breaks his obligation under the contract, he is said to have committed breach. Breach of contract may be actual or anticipatory. Actual breach may occur when performance is due or during performance. Anticipatory breach of contract occurs when a party refuses to perform before the time of performance.



THE CONSEQUENCES OF BREACH OF CONTRACT COMPENSATION FOR LOSS OR DAMAGE CAUSED BY BREACH OF CONTRACT

When a contract has been broken, the 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.

Compensation for failure to discharge obligation resembling those created by contract.—

When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and had broken his contract.

Explanation : In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

Illustrations

- (a) A contracts to sell and deliver 50 maunds of saltpetre to B, at a certain price to be paid on delivery. A breaks his promise. B is entitled to receive from A, by way of compensation, the sum, if any, by which the contract price falls short of the price for which B might have obtained 50 maunds of saltpetre of like quality at the time when the saltpetre ought to have been delivered.
- (b) A hires B's ship to go to Bombay, and there take on board on the first of January a cargo which A is to provide, and (bring it to Calcutta, the freight to be paid when earned. B's ship does not go to Bombay, but A has opportunities of procuring suitable conveyance for the cargo upon terms as advantageous as those on which he had chartered the ship. A avails himself of those opportunities, but is put to trouble and expense in doing so. A is entitled to receive compensation from B in respect of such trouble and expense.
- (c) A contracts to buy of B, at a stated price, 50 maunds of rice, no time being fixed for delivery. A afterwards informs B that he will not accept the rice if tendered to him. B is entitled to receive from A, by way of compensation, the amount, if any, by which the contract price exceeds that which B can obtain for the rice at the time when A informs B that he will not accept it.
- (d) A contracts to buy B's ship for 60,000 rupees, but breaks his promise. A must pay to B, by way of compensation, the excess, if any, of the contract price over the price which B can obtain for the ship at the time of the breach of promise.
- (e) A, the owner of a boat, contracts with B to take a cargo of jute to Mirzapur, for sale at that place, starting on a specified day. The boat, owing to some avoidable cause, does not start at the time appointed, whereby the arrival of the cargo at Mirzapur is delayed beyond the time when it would have arrived if the boat had sailed according to the contract. After that date, and before the arrival of the cargo, the price of jute falls. The measure of the compensation payable to B by A is the difference between the price which B could have obtained for the cargo at Mirzapur at the time when it would have arrived if forwarded in due course, and its market price at the time when it actually arrived.
- (f) A contracts to repair B's house in a certain manner, and receives payment in advance. A repairs the house, but not according to contract. B is entitled to recover from A the cost of making the repairs conforming to the contract.
- (g) A contracts to let his ship to B for a year, from the first of January, for a certain price. Freights rise, and, on the first of January, the hire obtainable for the ship is higher than the contract price. A breaks his promise. He must pay to B, by way of compensation, a sum equal to the difference between the contract price and the price for which B could hire a similar ship for a year on and from the first of January.
- (h) A contracts to supply B with a certain quantity of iron at a fixed price, being a higher price than that for which A could procure and deliver the iron. B wrongfully refuses to receive the iron. B must pay to A, by way of compensation, the difference between the contract price of the iron and the sum for which A could have obtained and delivered it.



- (i) A delivers to B, a common carrier, a machine to be conveyed, without delay, to A's mill, informing B that his mill is stopped for want of the machine. B unreasonably delays the delivery of the machine and A, in consequence, loses a profitable contract with the Government. A is entitled to receive from B, by way of compensation, the average amount of profit which would have been made by the working of the mill during the time that delivery of it was delayed, but not the loss sustained through the loss of the Government contract.
- (j) A, having contracted with B to supply B with 1,000 tons of iron at 100 rupees a ton, to be delivered at a stated time, contracts with C for the purchase of 1,000 tons of iron at 80 rupees a ton, telling C that he does so for the purpose of performing his contract with B. C fails to perform his contract with A, who cannot procure other iron, and B, in consequence, rescinds the contract. C must pay to A 20,000 rupees, being the profit which A would have made by the performance of his contract with B.
- (k) A contracts with B to make and deliver to B, by a fixed day, for a specified price, a certain piece of machinery. A does not deliver the piece of machinery at the time specified, and in consequence of this, B is obliged to procure another at a higher price than that which he was to have paid to A, and is prevented from performing a contract which B had made with a third person at the time of his contract with A (but which had not been then communicated to A), and is compelled to make compensation for breach of that contract. A must pay to B, by way of compensation, the difference between the contract price of the piece of machinery and the sum paid by B for another, but not the sum paid by B to the third person by way of compensation.
- (l) A, a builder, contracts to erect and finish a house by the first of January, in order that B may give possession of it at that time to C, to whom B has contracted to let it. A is informed of the contract between B and C. A builds the house so badly that, before the first of January, it falls down and has to be rebuilt by B, who, in consequence, loses the rent which he was to have received from C, and is obliged to make compensation to C for the breach of his contract. A must make compensation to B for the cost of rebuilding the house, for the rent lost, and for the compensation made to C.
- (m) A sells certain merchandise to B, warranting it to be of a particular quality, and B, in reliance upon this warranty, sells it to C with a similar warranty. The goods prove to be not according to the warranty, and B becomes liable to pay C a sum of money by way of compensation. B is entitled to be reimbursed this sum by A.
- (n) A contracts to pay a sum of money to B on a day specified A does not pay the money on that day; B in consequence of not receiving the money on that day is unable to pay his debts, and is totally ruined. A is not liable to make good to B anything except the principal sum he contracted to pay, together with interest up to the day of payment.
- (o) A contracts to deliver 50 maunds of saltpetre to B on the first of January, at a certain price. B afterwards, before the first day of January, contracts to sell the saltpetre to C at a price higher than the market price of the first of January. A breaks his promise. In estimating the compensation payable by A or to B, the market price of the first of January, and not the profit which would have arisen to B from the sale to C, is to be taken into account.
- (p) A contracts to sell and deliver 500 bales of cotton to B on a fixed day. A knows nothing of B's mode of conducting his business. A breaks his promise, and B, having no cotton, is obliged to close his mill. A is not responsible to B for the loss caused to B by the closing of the mill.
- (q) A contracts to sell and deliver to B, on the first of January, certain cloth which B intends to manufacture into caps of a particular kind, for which there is no demand, except at that season. The cloth is not delivered till after the appointed time, and too late to be used that year in making caps. B is entitled to receive from A, by way of compensation, the difference between the contract price of the cloth and its market price at the time of delivery, but not the profits which he expected to obtain by making caps, nor the expenses which he has been put to in making preparation for the manufacture.
- (r) A, a shipowner, contracts with B to convey him from Calcutta to Sydney in A's ship sailing on the first of January, and B pays to A, by way of deposit, one-half of his passage money. The ship does not sail on the first of January, and B, after being, in consequence, detained in Calcutta for some time, and thereby put to some expense, proceeds to Sydney in another vessel, and, in consequence, arriving too late in Sydney, loses a sum of money. A is liable to repay to B his deposit, with interest, and the expense to which



he is put by his detention in Calcutta, and the excess, if any, of the passage money paid for the second ship over that agreed upon for the first, but not the sum of money which B lost by arriving in Sydney too late.

COMPENSATION FOR BREACH OF CONTRACT WHERE PENALTY STIPULATED FOR

When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for.

Explanation: A stipulation for increased interest from the date of default may be a stipulation by way of penalty.

Exception: When any person enters into any bail-bond, recognizance or other instrument of the same nature, or, under the provisions of any law, or under the orders of the Central Government or of any State Government, gives any bond for the performance of any public duty or act in which the public are interested, he shall be liable, upon breach of the condition of any such instrument, to pay the whole sum mentioned therein.

Explanation: A person who enters into a contract with the Government does not necessarily thereby undertake any public duty, or promise to do an act in which the public are interested.

Illustrations

- (a) A contracts with B to pay B Rs. 1,000, if he fails to pay B Rs. 500 on a given day. A fails to pay B Rs. 500 on that day. B is entitled to recover from A such compensation, not exceeding Rs. 1,000, as the Court considers reasonable.
- (b) A contracts with B that if A practises as a surgeon within Calcutta, he will pay B Rs. 5,000. A practises as a surgeon in Calcutta. B is entitled to such compensation, not exceeding Rs. 5,000, as the Court considers reasonable.
- (c) A gives a recognizance binding him in a penalty of Rs. 500 to appear in Court on a certain day. He forfeits his recognizance. He is liable to pay the whole penalty.
- (d) A gives B a bond for the repayment of Rs. 1,000 with interest at 12 per cent at the end of six months, with a stipulation that, in case of default, interest shall be payable at the rate of 75 per cent from the date of default. This is a stipulation by way of penalty, and B is only entitled to recover from A such compensation as the Court considers reasonable.
- (e) A, who owes money to B, a money-lender, undertakes to repay him by delivering to him 10 maunds of grain on a certain date, and stipulates that, in the event of his not delivering the stipulated amount by the stipulated date, he shall be liable to deliver 20 maunds. This is a stipulation by way of penalty, and B is only entitled to reasonable compensation in case of breach.
- (f) A undertakes to repay B a loan of Rs. 1,000 by five equal monthly instalments, with a stipulation that, in default of payment of any instalment, the whole shall become due. This stipulation is not by way of penalty, and the contract may be enforced according to its terms.
- (g) A borrows Rs. 100 from B and gives him a bond for Rs. 200 payable by five yearly instalments of Rs. 40, with a stipulation that, in default of payment of any instalment, the whole shall become due. This is a stipulation by way of penalty.

PARTY RIGHTFULLY RESCINDING CONTRACT ENTITLED TO COMPENSATION

A person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through the non-fulfilment of the contract.

Illustration

A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B is entitled to claim compensation for the damage which he has sustained through the non-fulfilment of the contract.

**1.12 INDEMNITY AND GUARANTEE****“CONTRACT OF INDEMNITY” DEFINED**

A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a “contract of indemnity.”

Illustration

A contracts to indemnify B against the consequences of any proceedings which C may take against B in respect of a certain sum of 200 rupees. This is a contract of indemnity.

RIGHTS OF INDEMNITY-HOLDER WHEN SUED

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 it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorized him to bring or defend the suit;
- (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.

“CONTRACT OF GUARANTEE”, “SURETY”, “PRINCIPAL DEBTOR” AND “CREDITOR”

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 in respect of whose default the guarantee is given is called the “principal debtor”, and the person to whom the guarantee is given is called the “creditor”. A guarantee may be either oral or written.

CONSIDERATION FOR GUARANTEE

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.

Illustrations

- (a) 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 a sufficient consideration for C’s promise.
- (b) 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 a sufficient consideration for C’s promise.
- (c) A sells and delivers goods to B. C afterwards, without consideration, agrees to pay for them in default of B. The agreement is void.

SURETY’S LIABILITY

The liability of the surety is co-extensive with that of the principal debtor, unless it is otherwise provided by the contract.

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.



Distinction between Contract of Indemnity & Contract of Guarantee :

Contract of Indemnity	Contract of Guarantee
(i) There are two parties to a contract, indemnifier and indemnified.	There are three parties to contract, creditor, principal debtor and surety.
(ii) The liability of the indemnifier is primary and independent.	The liability of the surety is secondary and collateral, the principal debtor being primarily liable.
(iii) The number of contract is one, between indemnifier and indemnified.	The number of contract is three, (a) between principal debtor and creditor (b) between creditor and surety (c) between surety and principal debtor.
(iv) The liability of the indemnifier is subject to happening of a contingency.	There is an existing debt the performance of which is guaranteed by the surety.
(v) The indemnifier need not act only at the request of the indemnified.	The surety should give guarantee only at the request of the principal debtor.
(vi) The indemnifier cannot proceed against third parties in his own name unless there is an assignment in his favour.	After discharging the debt the surety can proceed against the principal debtor in his own name.

CONTINUING GUARANTEE

A guarantee which extends to a series of transactions is called a “continuing guarantee”.

Illustrations

- A, in consideration that B will employ C in collecting the rents of B's zamindari, promises B to be responsible, to the amount of 5,000 rupees, for due collection and payment by C of those rents. This is a continuing guarantee.
- A guarantees payment to B, a tea-dealer, to the amount of \$100, for any tea he may from time to time supply to C. B supplies C with tea to above the value of \$ 100, and C pays B for it. Afterwards B supplies C with tea to the value of \$200. C fails to pay. The guarantee given by A was a continuing guarantee, and he is accordingly liable to B to the extent of \$100.
- A guarantees payment to B of the price of five sacks of flour to be delivered by B to C and to be paid for in a month. B delivers five sacks to C. C pays for them. Afterwards B delivers four sacks to C, which C does not pay for. The guarantee given by A was not a continuing guarantee, and accordingly he is not liable for the price of the four sacks.

REVOCATION OF CONTINUING GUARANTEE

1. By Notice

A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor.

Illustrations

- A, in consideration of B's discounting, at A's request, bills of exchange for C, guarantees to B, for twelve months, the due payment of all such bills to the extent of 5,000 rupees. B discounts bills for C to the extent of 2,000 rupees. Afterwards, at the end of three months, A revokes the guarantee. This revocation discharges A from all liability to B for any subsequent discount. But A is liable to B for the 2,000 rupees, on default of C.
- A guarantees to B, to the extent of 10,000 rupees, that C shall pay all the bills that B shall draw upon him. B draws upon C. C accepts the bill. A gives notice of revocation. C dishonours the bill at maturity. A is liable upon his guarantee.

**2. By Surety's Death**

The death of the surety operates, in the absence of any contract to the contrary, as a revocation of a continuing guarantee, so far as regards future transactions.

3. By Other Modes

- (i) Novation
- ii) Variation in terms of contract
- (iii) Release of principal debtor
- (iv) Compounding with principal debtor
- (v) Creditor's act or omission impairing surety's eventual remedy
- (vi) Loss of security.

LIABILITY OF TWO PERSONS, PRIMARILY LIABLE, NOT AFFECTED BY ARRANGEMENT BETWEEN THEM THAT ONE SHALL BE SURETY ON OTHER'S DEFAULT

Where two persons contract with a third person to undertake a certain liability, and also contract with each other that one of them shall be liable only on the default of the other, the third person not being a party to such contract, the liability of each of such two persons to the third person under the first contract is not affected by the existence of the second contract, although such third person may have been aware of its existence.

Illustration

A and B make a joint and several promissory note to C. A makes it, in fact, as surety for B, and C knows this at the time when the note is made. The fact that A, to the knowledge of C, made the note as surety for B, is no answer to a suit by C against A upon the note.

DISCHARGE OF A SURETY**1. By revocation which may be by way of –**

- (i) giving notice
- (ii) death of surety
- (iii) novation i.e. substitution of with a new contract for an old one.

2. By conduct of creditor –**(i) By Variance in terms of contract**

Any variance, made without surety's consent, in the terms of the contract between the principal (debtor) and the creditor, discharges the surety as to transactions subsequent to the variance.

Illustrations

- (a) A becomes surety to C for B's conduct as a manager in C's bank. Afterwards, B and C contract, without A's consent, that B's salary shall be raised, and that he shall become liable for one-fourth of the losses on overdrafts. B allows a customer to overdraw, and the bank loses a sum of money. A is discharged from his suretyship by the variance made without his consent, and is not liable to make good this loss.
- (b) A guarantees C against the misconduct of B in an office to which B is appointed by C, and of which the duties are defined by an Act of the Legislature. By a subsequent Act, the nature of the office is materially altered. Afterwards, B misconducts himself. A is discharged by the change from future liability under his guarantee, though the misconduct of B is in respect of a duty not affected by the later Act.
- (c) C agrees to appoint B as his clerk to sell goods at a yearly salary, upon A's becoming surety to C for B's duly accounting for moneys received by him as such clerk. Afterwards, without A's knowledge or consent, C and B agree that B should be paid by a commission on the goods sold by him and not by a fixed salary. A is not liable for subsequent misconduct of B.
- (d) A gives to C a continuing guarantee to the extent of 3,000 rupees for any oil supplied by C to B on credit. Afterwards B becomes embarrassed, and, without the knowledge of A, B and C contract that C shall continue to supply B with oil for ready money, and that the payments shall be applied to the then existing debts between B and C. A is not liable on his guarantee for any goods supplied after this new arrangement.



- (e) C contracts to lend B 5,000 rupees on the 1st March. A guarantees repayment. C pays the 5,000 rupees to B on the 1st January. A is discharged from his liability, as the contract has been varied, inasmuch as C might sue B for the money before the 1st March.

(ii) By release or discharge of principal debtor

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

Illustrations

- (a) A gives a guarantee to C for goods to be supplied by C to B. C supplies goods to B, and afterwards B becomes embarrassed and contracts with his creditors (including C) to assign to them his property in consideration of their releasing him from their demands. Here B is released from his debt by the contract with C, and A is discharged from his suretyship.
- (b) A contracts with B to grow a crop of indigo on A's land and to deliver it to B at a fixed rate, and C guarantees A's performance of this contract. B diverts a stream of water which is necessary for irrigation of A's land and thereby prevents him from raising the indigo. C is no longer liable on his guarantee.
- (c) A contracts with B for a fixed price to build a house for B within a stipulated time, B supplying the necessary timber. C guarantees A's performance of the contract. B omits to supply the timber. C is discharged from his suretyship.

(iii) When creditor compounds with, gives time to, or agrees not to sue, principal debtor

A contract between the creditor and the principal debtor, by which the creditor makes a composition with, or promises to give time to, or not to sue, the principal debtor, discharges the surety, unless the surety assents to such contract.

SURETY NOT DISCHARGED WHEN AGREEMENT MADE WITH THIRD PERSON TO GIVE TIME TO PRINCIPAL DEBTOR

Where a contract to give time to the principal debtor is made by the creditor with a third person, and not with the principal debtor, the surety is not discharged.

Illustration

C, the holder of an overdue bill of exchange drawn by A as surety for B, and accepted by B, contracts with M to give time to B. A is not discharged.

CREDITOR'S FORBEARANCE TO SUE DOES NOT DISCHARGE SURETY

Mere forbearance on the part of the creditor to sue the principal debtor or to enforce any other remedy against him does not, in the absence of any provision in the guarantee to the contrary, discharge the surety.

Illustration

B owes to C a debt guaranteed by A. The debt becomes payable. C does not sue B for a year after the debt has become payable. A is not discharged from his suretyship.

RELEASE OF ONE CO-SURETY DOES NOT DISCHARGE OTHERS

Where there are co-sureties, a release by the creditor of one of them does not discharge the others; neither does it free the surety so released from his responsibility to the other sureties.

(iv) Discharge of Surety by Creditor's Act or Omission Impairing Surety's Eventual Remedy

If the creditor does any act which is inconsistent with the rights of the surety, or omits to do any 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.



Illustrations

- (a) B contracts to build a ship for C for a given sum, to be paid by instalments as the work reaches certain stages. A becomes surety to C for B's due performance of the contract. C, without the knowledge of A, prepays to B the last two instalments. A is discharged by this prepayment.
- (b) C lends money to B on the security of a joint and several promissory note made in C's favour by B, and by A as surety for B, together with a bill of sale of B's furniture, which gives power to C to sell the furniture, and apply the proceeds in discharge of the note. Subsequently, C sells the furniture, but, owing to his misconduct and wilful negligence, only a small price is realised. A is discharged from liability on the note.
- (c) A puts M as apprentice to B, and gives a guarantee to B for M's fidelity. B promises on his part that he will, at least once a month, see that M make up the cash. B omits to see this done as promised, and M embezzles. A is not liable to B on his guarantee.

3. By invalidation of contract:

- (i) *Guarantee Obtained by Misrepresentation Invalid* — Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid.
- (ii) *Guarantee Obtained by Concealment Invalid* — Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances is invalid.

Illustrations

- (a) A engages B as a clerk to collect money for him, B fails to account for some of his receipts, and A in consequence calls upon him to furnish security for his duly accounting. C gives his guarantee for B's duly accounting. A does not acquaint C with B's previous conduct. B afterwards makes default. The guarantee is invalid.
- (b) A guarantees to C payment for iron to be supplied by him to B to the amount of 2,000 tons. B and C have privately agreed that B should pay five rupees per ton beyond the market price, such excess to be applied in liquidation of an old debt. This agreement is concealed from A. A is not liable as a surety.
- (iii) *Guarantee on Contract that Creditor shall not Act on it until Co-Surety joins* — Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join.
- (iv) If there is failure of consideration between creditor and principal debtor.

RIGHTS OF A SURETY

1. Rights against Creditor

- (i) The surety may, before he is called upon to pay the debt, require the creditor to sue the principal debtor.
- (ii) On being sued by the creditor, the surety can rely on any counter claim the principal debtor has against the creditor.
- (iii) Where a guaranteed debt has become due, or default of the principal debtor to perform a guaranteed duty has taken place, the surety, upon payment or performance of all that he is liable for, is invested with all the rights which the creditor had against the principal debtor.
- (iv) *Surety's Right to benefit of Creditor's Securities*

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 loses, or, without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security.

Illustrations

- (a) C advances to B, his tenant, 2,000 rupees on the guarantee of A. C has also a further security for the 2,000 rupees by a mortgage of B's furniture. C cancels the mortgage. B becomes insolvent, and C sues A on his guarantee. A is discharged from liability to the amount of the value of the furniture.



- (b) C, a creditor, whose advance to B is secured by a decree, receives also a guarantee for that advance from A. C afterwards takes B's goods in execution under the decree, and then, without the knowledge of A, withdraws the execution. A is discharged.
- (c) A, as surety for B, makes a bond jointly with B to C, to secure a loan from C to B. Afterwards, C obtains from B a further security for the same debt. Subsequently, C gives up the further security. A is not discharged.

2. Rights against Principal Debtor

- (i) Right to be relieved of liability before payment has been made. But before he can do so, debt must be ascertained.
- (ii) **Implied promise to indemnify surety** — In every contract of guarantee there is an implied promise by the principal debtor to indemnify the surety; and the surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but no sums which he has paid wrongfully.

Illustrations

- (a) B is indebted to C, and A is surety for the debt. C demands payment from A, and on his refusal sues him for the amount. A defends the suit, having reasonable grounds for doing so, but is compelled to pay the amount of the debt with costs. He can recover from B the amount paid by him for costs, as well as the principal debt.
- (b) C lends B a sum of money, and A, at the request of B, accepts a bill of exchange drawn by B upon A to secure the amount. C, the holder of the bill, demands payment of it from A, and, on A's refusal to pay, sues him upon the bill. A, not having reasonable grounds for so doing, defends the suit, and has to pay the amount of the bill and costs. He can recover from B the amount of the bill, but not the sum paid for costs, as there was no real ground for defending the action.
- (c) A guarantees to C, to the extent of 2,000 rupees, payment for rice to be supplied by C to B. C supplies to B rice to a less amount than 2,000 rupees, but obtains from A payment of the sum of 2,000 rupees in respect of the rice supplied. A cannot recover from B more than the price of the rice actually supplied.

3. Right against Co-sureties (Right of contribution)

(i) Co-Sureties liable to contribute equally

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

Illustrations

- (a) A, B and C are sureties to D for the sum of 3,000 rupees lent to E. E makes default in payment. A, B and C are liable, as between themselves, to pay 1,000 rupees each.
- (b) A, B and C are sureties to D for the sum of 1,000 rupees lent to E, and there is a contract between A, B and C that A is to be responsible to the extent of one-quarter, B to the extent of one-quarter, and C to the extent of one-half. E makes default in payment. As between the sureties, A is liable to pay 250 rupees, B 250 rupees, and C 500 rupees.

(ii) Liability of co-sureties bound in different sums

Co-sureties who are bound in different sums are liable to pay equally as far as the limits of their respective obligations permit.

Illustrations

- (a) A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 30,000 rupees. A, B and C are each liable to pay 10,000 rupees.
- (b) A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly



accounting to E. D makes default to the extent of 40,000 rupees; A is liable to pay 10,000 rupees, and B and C 15,000 rupees each.

- (c) A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 70,000 rupees. A, B and C have to pay each the full penalty of his bond.

(iii) A release by creditor of one of the co-sureties, doesnot discharge the others, nor does it free the co-surety so released, from his responsibility to other sureties.

1.13 BAILMENT

“BAILMENT”, “BAILOR” AND “BAILEE”

A “bailment” is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person delivering the goods is called the “bailor”. The person to whom they are delivered is called the “bailee”.

Explanation : If a person already in possession of the goods of another contract to hold them as a bailee, he thereby becomes the bailee, and the owner becomes the bailor, of such goods, although they may not have been delivered by way of bailment.

From the definition it is clear that ‘bailment’ is concerned only with goods.

DELIVERY TO BAILEE HOW MADE

The delivery to the bailee may be made by doing anything which has the effect of putting the goods in the possession of the intended bailee or of any person authorized to hold them on his behalf.

Consideration for bailment : The detriment suffered by the bailor, in parting with the possession of the goods, is sufficient consideration to support the contract of bailment.

BAILOR'S DUTY TO DISCLOSE FAULTS IN GOODS BAILED

The bailor is bound to disclose to the bailee faults in the goods bailed, of which the bailor is aware, and which materially interfere with the use of them, or expose the bailee to extraordinary risks; and if he does not make such disclosure, he is responsible for damage arising to the bailee directly from such faults.

If the goods are bailed for hire, the bailor is responsible for such damage, whether he was or was not aware of the existence of such faults in the goods bailed.

Illustrations

- (a) A lends a horse, which he knows to be vicious, to B. He does not disclose the fact that the horse is vicious. The horse runs away. B is thrown and injured. A is responsible to B for damage sustained.
- (b) A hires a carriage of B. The carriage is unsafe, though B is not aware of it, and A is injured. B is responsible to A for the injury.

CARE TO BE TAKEN BY BAILEE

In all cases of bailment the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take of his own goods of the same bulk, quality and value as the goods bailed.

BAILEE WHEN NOT LIABLE FOR LOSS, ETC., OF THING BAILED

The bailee, in the absence of any special contract, is not responsible for the loss, destruction or deterioration of the thing bailed, if he has taken the amount of care of it described in section 151.

TERMINATION OF BAILMENT BY BAILEE'S ACT INCONSISTENT WITH CONDITIONS

A contract of bailment is voidable at the option of the bailor, if the bailee does any act with regard to the goods bailed, inconsistent with the conditions of the bailment.



Illustration

A lets to B, for hire, a horse for his own riding. B drives the horse in his carriage. This is, at the option of A, a termination of the bailment.

LIABILITY OF BAILEE MAKING UNAUTHORISED USE OF GOODS BAILED

If the bailee makes any use of the goods bailed, which is not according to the conditions of the bailment, he is liable to make compensation to the bailor for any damage arising to the goods from or during such use of them.

Illustrations

- (a) A lends a horse to B for his own riding only. B allows C, a member of his family, to ride the horse. C rides with care, but the horse accidentally falls and is injured. B is liable to make compensation to A for the injury done to the horse.
- (b) A hires a horse in Calcutta from B expressly to march to Benares. A rides with due care, but marches to Cuttack instead. The horse accidentally falls and is injured. A is liable to make compensation to B for the injury to the horse.

EFFECT OF MIXTURE, WITH BAILOR'S CONSENT, OF HIS GOODS WITH BAILEE'S

If the bailee, with 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.

EFFECT OF MIXTURE, WITHOUT BAILOR'S CONSENT, WHEN THE GOODS CAN BE SEPARATED

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 or division, and any damage arising from the mixture.

Illustration

A bails 100 bales of cotton marked with a particular mark to B. B, without A's consent, mixes the 100 bales with other bales of his own, bearing a different mark; A is entitled to have his 100 bales returned, and B is bound to bear all the expenses incurred in the separation of the bales, and any other incidental damage.

EFFECT OF MIXTURE, WITHOUT BAILOR'S CONSENT, WHEN THE GOODS CANNOT BE SEPARATED

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 the goods.

Illustration

A bails a barrel of Cape flour worth Rs. 45 to B. B, without A's consent, mixes the flour with country flour of his own, worth only Rs. 25 a barrel. B must compensate A for the loss of his flour.

REPAYMENT BY BAILOR OF NECESSARY EXPENSES

Where, by the conditions of the bailment, the goods are to be kept or to be carried, or to have work done upon them by the bailee for the bailor, and the bailee is to receive no remuneration, the bailor shall repay to the bailee the necessary expenses incurred by him for the purpose of the bailment.

RESTORATION OF GOODS LENT GRATUITOUSLY

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 face 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 for the amount in which the loss so occasioned exceeds the benefit so derived.

RETURN OF GOODS BAILED ON EXPIRATION OF TIME OR ACCOMPLISHMENT OF PURPOSE

It is the duty of bailee to return, or deliver according to the bailor's directions, the goods bailed without demand, as soon as the time for which they were bailed, has expired, or the purpose for which they were bailed has been accomplished.

**BAILEE'S RESPONSIBILITY WHEN GOODS ARE NOT DULY RETURNED**

If, by the default of the bailee, the goods are not returned, delivered or tendered at the proper time, he is responsible to the bailor for any loss, destruction or deterioration of the goods from that time.

TERMINATION OF GRATUITOUS BAILMENT BY DEATH.

A gratuitous bailment is terminated by the death either of the bailor or of the bailee.

BAILOR ENTITLED TO INCREASE OR PROFIT FROM GOODS BAILED

In the absence of any contract to the contrary, the bailee is bound to deliver to the bailor, or according to his directions, any increase or profit which may have accrued from the goods bailed.

Illustration

A leaves a cow in the custody of B to be taken care of. The cow has a calf, B is bound to deliver the calf as well as the cow to A.

BAILOR'S RESPONSIBILITY TO BAILEE

The bailor is responsible to the bailee for any loss which the bailee may sustain by reason that the bailor was not entitled to make the bailment, or to receive back the goods or to give directions, respecting them.

BAILMENT BY SEVERAL JOINT OWNERS

If several joint owners of goods bail them, the bailee may deliver them back to, or according to the directions of, one joint owner without the consent of all, in the absence of any agreement to the contrary.

BAILEE NOT RESPONSIBLE ON REDELIVERY TO BAILOR WITHOUT TITLE

If the bailor has no title to the goods, and the bailee, in good faith, delivers them back to, or according to the directions of, the bailor, the bailee is not responsible to the owner in respect of such delivery.

RIGHT OF THIRD PERSON CLAIMING GOODS BAILED

If a person, other than the bailor, claims goods bailed, he may apply to the Court to stop the delivery of the goods to the bailor, and to decide the title to the goods.

RIGHT OF FINDER OF GOODS; MAY SUE FOR-SPECIFIC REWARD OFFERED

The finder of goods has no right to sue the owner for compensation for trouble and expense voluntarily incurred by him to preserve the goods and to find out the owner; but he may retain the goods against the owner until he receives such compensation; and, where the owner has offered a specific reward for the return of goods lost, the finder may sue for such reward, and may retain the goods until he receives it.

WHEN FINDER OF THING COMMONLY ON SALE MAY SELL IT

When a thing which is commonly the subject of sale is lost, if the owner cannot with reasonable diligence be found, or if he refuses, upon demand, to pay the lawful charges of the finder, the finder may sell it—

- (1) when the thing is in danger of perishing or of losing the greater part of its value, or
- (2) when the lawful charges of the finder in respect of the thing found amount to two-thirds of its value.

BAILEE'S PARTICULAR LIEN

'Lien' means right of a person to retain possession of some goods belonging to another until claim of the person in possession is satisfied.

Where the bailee has, in accordance with the purpose of the bailment, rendered any service involving the exercise of labour or skill in respect of the goods bailed, he has, in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them.

Illustrations

- (a) A delivers a rough diamond to B, a jeweller, to be cut and polished, which is accordingly done. B is entitled to retain the stone till he is paid for the services he has rendered.



- (b) A gives cloth to B, a tailor, to make into a coat. B promises A to deliver the coat as soon as it is finished, and to give a three-months' credit for the price. B is not entitled to retain the coat until he is paid.

GENERAL LIEN OF BANKERS, FACTORS, WHARFINGERS, ATTORNEYS AND POLICY-BROKERS

Bankers, factors, wharfingers, attorneys of a High Court and policy-brokers may, in the absence of a contract to the contrary, retain, as a security for a general balance of account any goods bailed to them; but no other persons have a right to retain, as a security for such balance, goods bailed to them, unless there is an express contract to the effect.

1.14 BAILMENT OF PLEDGES

“PLEDGE”, “PAWNOR” AND “PAWNEE”

The bailment of goods as security for payment of a debt or performance of a promise is called “pledge”. The bailor is in this case called the “pawnor”. The bailee is called the “pawnee”.

PAWNEE'S RIGHT OF RETAINER

The pawnee may retain the goods pledged, not only for payment of the debt or the performance of the promise, but for the interest, of the debt, and all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged.

PAWNEE NOT TO RETAIN FOR DEBT OR PROMISE OTHER THAN THAT FOR WHICH GOODS PLEDGED. PRESUMPTION IN CASE OF SUBSEQUENT ADVANCES

The pawnee shall not, in the absence of a contract to that effect retain the goods pledged for any debt or promise other than the debt or promise for which they are pledged; but such contract, in the absence of anything to the contrary, shall be presumed in regard to subsequent advances made by the pawnee.

PAWNEE'S RIGHT AS TO EXTRAORDINARY EXPENSES INCURRED

The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged.

PAWNEE'S RIGHT WHERE PAWNOR MAKES DEFAULT

If the pawnor makes default in payment of the debt, or performance, at the stipulated time, of the promise, in respect of which the goods were pledged, the pawnee may bring a suit against the pawnor upon the debt or promise, and retain the goods pledged as a collateral security; or he may sell the thing pledged on giving the pawnor reasonable notice of the sale.

If the proceeds of such sale are less than the amount due in respect of the debt or promise, the pawnor is still liable to pay the balance. If the proceeds of the sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnor.

DEFAULTING PAWNOR'S RIGHT TO REDEEM

If a time is stipulated for the payment of the debt, or performance of the promise, for which the pledge is made, and the pawnor makes default in payment of the debt or performance of the promise at the stipulated time, he may redeem the goods pledged at any subsequent time before the actual sale of them; but he must, in that case, pay, in addition, any expenses which have arisen from his default.

PLEDGE BY NON-OWNERS

1. Pledge by 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, shall be as valid as if he were expressly authorised by the owner of the goods to make the same; provided that the pawnee acts in good faith and has not at the time of the pledge notice that the pawnor has no authority to pledge.

Explanation : In this section, the expressions ‘mercantile agent’ and ‘documents of title’ shall have the meanings assigned to them in the Indian Sale of Goods Act, 1930.



2. Pledge by person in possession under voidable contract — When the pawnor has obtained possession of the goods pledged by him under a contract voidable under section 19 or section 19A, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title.

3. Pledge where pawnor has only a limited interest — Where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest.

4. Pledge by seller after or buyer before sale can create a valid pledge provided the pawnee acts in good faith and has no notice of previous sale of goods to the buyer or lien of seller on the goods.

5. Pledge by co-owner in possession thereof with consent of other co-owners may create a valid pledge.

SUIT BY BAILOR OR BAILEE AGAINST WRONG-DOER

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

APPORTIONMENT OF RELIEF OR COMPENSATION OBTAINED BY SUCH SUITS

Whatever is obtained by way of relief or compensation in any such suit shall, as between the bailor and the bailee, be dealt with according to their respective interests.

1.15 CONTRACTS OF AGENCY

AGENT

An “agent” is a person employed to do any act for another or to represent another in dealings with third persons. The person for whom such act is done, or who is so represented, is called the “principal”. The function of agent is to bring his principle in contact with third person.

RULES OF AGENCY

- (i) Subject to certain acts personal in nature like marriage, whatever a person can do , he can do so through an agent.
- (ii) He who acts through an agent , does it himself subject to certain conditions.

WHO MAY EMPLOY AGENT

Any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent.

WHO MAY BE AN AGENT

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

CONSIDERATION NOT NECESSARY

No consideration is necessary to create an agency.

CREATION OF AGENCY

1. By express agreement : The usual form of a contract of agency is a power of attorney on a stamped paper.

2. By implied agreement : Such agency arises when the principal through his conduct leads the third party to believe that certain person is his agent. It includes-

- (i) Agency by estoppel
- (ii) Agency by holding out
- (iii) Agency by necessity



3. By ratification : When a person acts on behalf of another without his consent , and the other person accepts his acts, the acts are said to be ratified. This places the parties in the same position in which they would have been if acts were done with prior authority.

EFFECT OF RATIFICATION

Where acts are done by one person on behalf of another, but without his knowledge or authority, he may elect to ratify or to disown such acts. If he ratifies them, the same effects will follow as if they had been performed by his authority.

RATIFICATION MAY BE EXPRESSED OR IMPLIED

Ratification may be expressed or may be implied in the conduct of the person on whose behalf the acts are done.

Illustrations

- (a) A, without authority, buys goods for B. Afterwards B sells them to C on his own account; B's conduct implies a ratification of the purchase made for him by A.
- (b) A, without B's authority, lends B's money to C. Afterwards B accepts interests on the money from C. B's conduct implies a ratification of the loan.

KNOWLEDGE REQUISITE FOR VALID RATIFICATION.

No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.

EFFECT OF RATIFYING UNAUTHORIZED ACT FORMING PART OF A TRANSACTION

A person ratifying any unauthorized act done on his behalf ratifies the whole of the transaction of which such act formed a part.

RATIFICATION OF UNAUTHORIZED ACT CANNOT INJURE THIRD PERSON

An act done by one person on behalf of another, without such other person's authority, which, if done with authority, would have the effect of subjecting a third person to damages, or of terminating any right or interest of a third person, cannot, by ratification, be made to have such effect.

Illustrations

- (a) A, not being authorized thereto by B, demands on behalf of B, the delivery of a chattel, the property of B, from C, who is in possession of it. This demand cannot be ratified by B, so as to make C liable for damages for his refusal to deliver.
- (b) A holds a lease from B, terminable on three months' notice. C, an unauthorized person, gives notice of termination to A. The notice cannot be ratified by B, so as to be binding on A.

4. By operation of law : Sometimes agency arises due to operation of law. Promoters of a company and partners of a firm are agents due to such implication.

AGENT'S AUTHORITY MAY BE EXPRESS OR IMPLIED

The authority of an agent may be express or implied.

DEFINITIONS OF EXPRESS AND IMPLIED AUTHORITY.

An authority is said to be express when it is given by words, spoken or written. An authority is said to be implied when it is to be inferred from the circumstances of the case; and things spoken or written, or the ordinary course of dealing, may be accounted circumstances of the case.

Illustration

A owns a shop in Serampore, living himself in Calcutta, and visiting the shop occasionally. The shop is managed by B, and he is in the habit of ordering goods from C in the name of A for the purposes of the shop, and of paying for them out of A's funds with A's knowledge. B has an implied authority from A to order goods from C in the name of A for the purposes of the shop.

An agent having an authority to carry on a business has authority to do every lawful thing necessary for the purpose, or usually done in the course, of conducting such business.

- (a) A is employed by B, residing in London, to recover at Bombay a debt due to B. A may adopt any legal process necessary for the purpose of recovering the debt, and may give a valid discharge for the same.
- (b) A constitutes B as his agent to carry on his business of a shipbuilder. B may purchase timber and other materials, and hire workmen, for the purposes of carrying on the business.

- (a) An agent for sale may have goods repaired if it be necessary.
- (b) A consigns provisions to B at Calcutta, with directions to send them immediately to C at Cuttack. B may sell the provisions at Calcutta, if they will not bear the journey to Cuttack without spoiling.

(a) A directs B, his solicitor, to sell his estate by auction, and to employ an auctioneer for the purpose. B names C, an auctioneer, to conduct the sale. C is not a sub-agent, but is A's agent for the conduct of the sale.



- (b) A authorizes B, a merchant in Calcutta, to recover the moneys due to A from C & Co. B instructs D, a solicitor, to take legal proceedings against C & Co. for the recovery of the money. D is not a sub-agent, but is a solicitor for A.

AGENT'S DUTY IN NAMING SUCH PERSON

In selecting such agent for his principal, an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case; and, if he does this, he is not responsible to the principal for the acts or negligence of the agent so selected.

Illustrations

- (a) A instructs B, a merchant, to buy a ship for him. B employs a ship surveyor of good reputation to choose a ship for A. The surveyor makes the choice negligently and the ship turns out to be unseaworthy and is lost. B is not, but the surveyor is, responsible to A.
- (b) A consigns goods to B, a merchant, for sale. B, in due course, employs an auctioneer in good credit to sell the goods of A, and allows the auctioneer to receive the proceeds of the sale. The auctioneer afterwards becomes insolvent without having accounted for the proceeds. B is not responsible to A for the proceeds.

TERMINATION OF AGENCY

An agency is terminated by the principal revoking his authority; or by the agent renouncing the business of the agency; or by the business of the agency being completed; or by either the principal or agent dying or becoming of unsound mind; or by the principal being adjudicated an insolvent under the provisions of any Act for the time being in force for the relief of insolvent debtors.

1. BY ACT OF PARTIES

- (i) Agreement between principal and agent.
- (ii) **Revocation by the principal** : The principal may revoke the authority of the agent any time before the authority has been exercised. When agency is continuous one, notice of termination to agent as well as third parties is essential.

The principal cannot revoke the authority given to his agent after the authority has been partly exercised so far as regards such acts and obligations as arise from acts already done in the agency.

Illustrations

- (a) A authorizes B to buy 1,000 bales of cotton on account of A, and to pay for it out of A's money remaining in B's hands. B buys 1,000 bales of cotton in his own name, so as to make himself personally liable for the price. A cannot revoke B's authority so far as regards payment for the cotton.
- (b) A authorizes B to buy 1,000 bales of cotton on account of A, and to pay for it out of A's money remaining in B's hands. B buys 1,000 bales of cotton in A's name, and so as not to render himself personally liable for the price. A can revoke B's authority to pay for the cotton.
- (iii) Agency may also be revoked by an agent by express renunciation after giving reasonable notice to principal.

COMPENSATION FOR REVOCATION BY PRINCIPAL, OR RENUNCIATION BY AGENT

Where there is an express or implied contract that the agency should be continued for any period of time, the principal must make compensation to the agent, or the agent to the principal, as the case may be, for any previous revocation or renunciation of the agency without sufficient cause.

NOTICE OF REVOCATION OR RENUNCIATION

Reasonable notice must be given of such revocation or renunciation; otherwise the damage thereby resulting to the principal or the agent, as the case may be, must be made good to the one by the other.

REVOCATION AND RENUNCIATION MAY BE EXPRESSED OR IMPLIED

Revocation and renunciation may be expressed or may be implied in the conduct of the principal or agent respectively.

**Illustration**

A empowers B to let A's house. Afterwards A lets it himself. This is an implied revocation of B's authority.

2. BY OPERATION OF LAW :

- (i) Performance of contract.
- (ii) Expiry of time period for which the agent was appointed even if the work is incomplete.
- (iii) Death or insanity of principal or agent.
- (iv) Insolvency of principal or agent
- (v) Destruction of subject matter.
- (vi) Dissolution of company whether it is principal or agent.
- (vii) When the countries of principal and agent breaks into a war.
- (viii) Sub-agents' authority is terminated on termination of authority of the agent.

WHEN TERMINATION OF AGENT'S AUTHORITY TAKES EFFECT AS TO AGENT, AND AS TO THIRD PERSONS

The termination of the authority of an agent does not, so far as regards the agent, take effect before it becomes known to him, or, so far as regards third persons, before it becomes known to them.

Illustrations

- (a) A directs B to sell goods for him, and agrees to give B five per cent commission on the price fetched by the goods. A afterwards, by letter, revokes B's authority. B, after the letter is sent, but before he receives it, sells the goods for 100 rupees. The sale is binding on A, and B is entitled to five rupees as his commission.
- (b) A, at Madras, by letter directs B to sell for him some cotton lying in a warehouse in Bombay, and afterwards, by letter, revokes his authority to sell, and directs B to send the cotton to Madras. B, after receiving the second letter, enters into a contract with C, who knows of the first letter, but not of the second, for the sale to him of the cotton. C pays B the money, with which B absconds. C's payment is good as against A.
- (c) A directs B, his agent, to pay certain money to C. A dies, and D takes out probate to his will. B, after A's death, but before hearing of it, pays the money to C. The payment is good as against D, the executor.

TERMINATION OF AGENCY, WHERE AGENT HAS AN INTEREST IN SUBJECT-MATTER

Where the agent has himself an interest in the property which forms the subject-matter of the agency, the agency cannot, in the absence of an express contract, be terminated to the prejudice of such interest.

Illustrations

- (a) A gives authority to B to sell A's land, and to pay himself, out of the proceeds, the debts due to him from A. A cannot revoke this authority, nor can it be terminated by his insanity or death.
- (b) A consigns 1,000 bales of cotton to B, who has made advances to him on such cotton, and desires B to sell the cotton, and to repay himself, out of the price the amount of his own advances. A cannot revoke this authority, nor is it terminated by his insanity or death.

AGENT'S DUTY ON TERMINATION OF AGENCY BY PRINCIPAL'S DEATH OR INSANITY

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 interests entrusted to him.

TERMINATION OF SUB-AGENT'S AUTHORITY

The termination of the authority of an agent causes the termination (subject to the rules herein contained regarding the termination of an agent's authority) of the authority of all sub-agents appointed by him.



DUTIES OF AGENT

1. To carry out work as per direction of Principal

An agent is bound to conduct the business of his principal according to the directions given by the principal, or, in the absence of any such directions, according to the custom which prevails in doing business of the same kind at the place where the agent conducts such business. When the agent acts otherwise, if any loss be sustained, he must make it good to his principal, and, if any profit accrues, he must account for it.

Illustrations

- (a) A, an agent engaged in carrying on for B a business, in which it is the custom to invest from time to time, at interest, the moneys which may be in hand, omits to make such investment. A must make good to B the interest usually obtained by such investments.
- (b) B, a broker, in whose business it is not the custom to sell on credit, sells goods of A on credit to C, whose credit at the time was very high. C, before payment, becomes insolvent. B must make good the loss to A.

2. To carry out with care, skill & diligence

An agent is bound to conduct the business of the agency with as much skill as is generally possessed by persons engaged in similar business, unless the principal has notice of his want of skill. The agent is always bound to act with reasonable diligence, and to use such skill as he possesses; and to make compensation to his principal in respect of the direct consequences of his own neglect, want of skill or misconduct, but not in respect of loss or damage which are indirectly or remotely caused by such neglect, want of skill or misconduct.

Illustrations

- (a) A, a merchant in Calcutta, has an agent, B, in London, to whom a sum of money is paid on A's account, with orders to remit. B retains the money for a considerable time. A, in consequence of not receiving the money, becomes insolvent. B is liable for the money and interest from the day on which it ought to have been paid, according to the usual rate, and for any further direct loss — as, e.g., by variation of rate of exchange— but not further.
- (b) A, an agent for the sale of goods, having authority to sell on credit, sells to B on credit, without making the proper and usual enquiries as to the solvency of B. B, at the time of such sale, is insolvent. A must make compensation to his principal in respect of any loss thereby sustained.
- (c) A, an insurance-broker, employed by B to effect an insurance on a ship, omits to see that the usual clauses are inserted in the policy. The ship is afterwards lost. In consequence of the omission of the clauses nothing can be recovered from the underwriters. A is bound to make good the loss to B.
- (d) A, a merchant in England, directs B, his agent at Bombay, who accepts the agency, to send him 100 bales of cotton by a certain ship. B, having it in his power to send the cotton, omits to do so. The ship arrives safely in England. Soon after her arrival the price of cotton rises. B is bound to make good to A the profit which he might have made by the 100 bales of cotton at the time the ship arrived, but not any profit he might have made by the subsequent rise.

3. An agent is bound to render proper accounts to his principal on demand.

4. It is the duty of an agent, in cases of difficulty, to use all reasonable diligence in communicating with his principal, and in seeking to obtain his instructions.

5. Not to deal in his own account :

If an agent deals on his own account in the business of the agency, without first obtaining the consent of his principal and acquainting him with all material circumstances which have come to his own knowledge on the subject, the principal may repudiate the transaction, if the case shows either that any material fact has been dishonestly concealed from him by the agent, or that the dealings of the agent have been disadvantageous to him.

Illustrations

- (a) A directs B to sell A's estate. B buys the estate for himself in the name of C. A, on discovering that B has bought the estate for himself, may repudiate the sale, if he can show that B has dishonestly concealed any material fact, or that the sale has been disadvantageous to him.



- (b) A directs B to sell A's estate. B, on looking over the estate before selling it, finds a mine on the estate which is unknown to A. B informs A that he wishes to buy the estate for himself, but conceals the discovery of the mine. A allows B to buy, in ignorance of the existence of the mine. A, on discovering that B knew of the mine at the time he bought the estate, may either repudiate or adopt the sale at his option.

PRINCIPAL'S RIGHT TO BENEFIT GAINED BY AGENT DEALING ON HIS OWN ACCOUNT IN BUSINESS OF AGENCY

If an agent, without the knowledge of his principal, deals in the business of the agency on his own account instead of on account of his principal, the principal is entitled to claim from the agent any benefit which may have resulted to him from the transaction.

Illustration

A directs B, his agent, to buy a certain house for him. B tells A it cannot be bought, and buys the house for himself. A may, on discovering that B has bought the house, compel him to sell it to A at the price he gave for it.

AGENT'S RIGHT OF RETAINER OUT OF SUMS RECEIVED ON PRINCIPAL'S ACCOUNT

An agent may retain, out of any sums received on account of the principal in the business of the agency, all moneys due to himself in respect of advances made or expenses properly incurred by him in conducting such business, and also such remuneration as may be payable to him for acting as agent.

6. Agent's duty to pay sums received for principal

Subject to such deductions, the agent is bound to pay to his principal all sums received on his account.

7. To protect and preserve the interest of principal in case of his death or insanity.
8. An agent should not use information obtained in course of agency against the principal.
9. He must not set an adverse title to the goods.
10. He should not put himself in a position where his duties and interest will conflict.
11. He must not delegate his authority subject to certain exceptions.

RIGHTS OF AGENT

1. AGENT'S LIEN ON PRINCIPAL'S PROPERTY

In the absence of any contract to the contrary, an agent is entitled to retain goods, papers, and other property, whether movable or immovable, of the principal received by him, until the amount due to himself for commission, disbursements and services in respect of the same has been paid or accounted for to him.

2. Right to receive remuneration as per agreement, or if there is no agreement, reasonable remuneration.

WHEN AGENT'S REMUNERATION BECOMES DUE

In the absence of any special contract, payment for the performance of any act is not due to the agent until the completion of such act; but an agent may detain moneys received by him on account of goods sold, although the whole of the goods consigned to him for sale may not have been sold, or although the sale may not be actually complete.

AGENT NOT ENTITLED TO REMUNERATION FOR BUSINESS MISCONDUCTED

An agent who is guilty of misconduct in the business of the agency is not entitled to any remuneration in respect of that part of the business which he has misconducted.

Illustrations

- (a) A employs B to recover 1,00,000 rupees from C, and to lay it out on good security. B recovers the 1,00,000 rupees and lays out 90,000 rupees on good security, but lays out 10,000 rupees on security which he ought to have known to be bad, whereby A loses 2,000 rupees. B is entitled to remuneration for recovering the 1,00,000 rupees and for investing the 90,000 rupees. He is not entitled to any remuneration for investing the 10,000 rupees, and he must make good the 2,000 rupees to B.
- (b) A employs B to recover 1,000 rupees from C. Through B's misconduct the money is not recovered. B is entitled to no remuneration for his services, and must make good the loss.



3. The agent has right to be indemnified against all lawful acts done by him in exercise of authority conferred upon him.
4. The agent has right to be compensated for all injuries sustained by him because of negligence or lack of skill on part of principal.
5. The agent has 'right of stoppage in transit' under following circumstances:
 - (i) If he has bought goods on behalf of principal incurring personal liability. This right is similar to that of an unpaid seller.
 - (ii) If he is personally liable to principal for price of goods sold, he has this right against buyer in case the buyer becomes insolvent. This right is also similar to that of an unpaid seller.

PRINCIPAL'S DUTY TO AGENT

(1) AGENT TO BE INDEMNIFIED AGAINST CONSEQUENCES OF LAWFUL ACTS

The employer of an agent is bound to indemnify him against the consequences of all lawful acts done by such agent in exercise of the authority conferred upon him.

Illustrations

- (a) B, at Singapore, under instructions from A of Calcutta, contracts with C to deliver certain goods to him. A does not send the goods to B, and C sues B for breach of contract. B informs A of the suit, and A authorizes him to defend the suit. B defends the suit, and is compelled to pay damages and costs, and incurs expenses. A is liable to B for such damages, costs and expenses.
- (b) B, a broker at Calcutta, by the orders of A, a merchant there, contracts with C for the purchase of 10 casks of oil for A. Afterwards A refuses to receive the oil, and C sues B. B informs A, who repudiates the contract altogether. B defends, but unsuccessfully, and has to pay damages and costs and incurs expenses. A is liable to B for such damages, costs and expenses.

(2) AGENT TO BE INDEMNIFIED AGAINST CONSEQUENCES OF ACTS DONE IN GOOD FAITH

Where one person employs another to do an act, and the agent does the act in good faith, the employer is liable to indemnify the agent against the consequences of that act, though it causes an injury to the rights of third persons.

Illustrations

- (a) A, a decree-holder and entitled to execution of B's goods, requires the officer of the Court to seize certain goods, representing them to be the goods of B. The officer seizes the goods, and is sued by C, the true owner of the goods. A is liable to indemnify the officer for the sum which he is compelled to pay to C, in consequence of obeying A's directions.
- (b) B, at the request of A, sells goods in the possession of A, but which A had no right to dispose of. B does not know this, and hands over the proceeds of the sale to A. Afterwards C, the true owner of the goods, sues B and recovers the value of the goods and costs. A is liable to indemnify B for what he has been compelled to pay to C and for B's own expenses.

NON-LIABILITY OF EMPLOYER OF AGENT TO DO A CRIMINAL ACT

Where one person employs another to do an act which is criminal, the employer is not liable to the agent, either upon an express or an implied promise, to indemnify him against the consequences of that act.

Illustrations

- (a) A employs B to beat C, and agrees to indemnify him against all consequences of the act. B thereupon beats C, and has to pay damages to C for so doing. A is not liable to indemnify B for those damages.
- (b) B, the proprietor of a newspaper, publishes, at A's request, a libel upon C in the paper, and A agrees to indemnify B against the consequences of the publication, and all costs and damages of any action in respect thereof. B is sued by C and has to pay damages, and also incurs expenses. A is not liable to B upon the indemnity.

**EFFECT OF AGENCY ON CONTRACT WITH THIRD PERSONS ENFORCEMENT AND CONSEQUENCES OF AGENT'S CONTRACTS**

Contracts entered into through an agent, and obligations arising from acts done by an agent, may be enforced in the same manner, and will have the same legal consequences, as if the contracts had been entered into and the acts done by the principal in person.

Illustrations

- (a) A buys goods from B, knowing that he is an agent for their sale, but not knowing who is the principal. B's principal is the person entitled to claim from A the price of the goods, and A cannot, in a suit by the principal, set off against that claim a debt due to himself from B.
- (b) A, being B's agent with authority to receive money on his behalf, receives from C, a sum of money due to B. C is discharged of his obligation to pay the sum in question to B.

(3) COMPENSATION TO AGENT FOR INJURY CAUSED BY PRINCIPAL'S NEGLIGENCE

The principal must make compensation to his agent in respect of injury caused to such agent by the principal's neglect or want of skill.

Illustration

A employs B as a bricklayer in building a house, and puts up the scaffolding himself. The scaffolding is unskillfully put up, and B is in consequence hurt. A must make compensation to B.

PRINCIPAL HOW FAR BOUND, WHEN AGENT EXCEEDS AUTHORITY

When an agent does more than he is authorised to do, and when the part of what he does, which is within his authority, can be separated from the part which is beyond his authority, so much only of what he does as is within his authority is binding as between him and his principal.

Illustration

A, being owner of a ship and cargo, authorizes B to procure an insurance for 4,000 rupees on the ship. B procures a policy for 4,000 rupees on the ship, and another for the like sum on the cargo. A is bound to pay the premium for the policy on the ship, but not the premium for the policy on the cargo.

PRINCIPAL NOT BOUND WHEN EXCESS OF AGENT'S AUTHORITY IS NOT SEPARABLE

Where an agent does more than he is authorised to do, and what he does beyond the scope of his authority cannot be separated from what is within it, the principal is not bound to recognise the transaction.

Illustration

A authorizes B to buy 500 sheep for him. B buys 500 sheep and 200 lambs for one sum of 6,000 rupees. A may repudiate the whole transaction.

CONSEQUENCES OF NOTICE GIVEN TO AGENT

Any notice given to or information obtained by the agent, provided it be given or obtained in the course of the business transacted by him for the principal, shall, as between the principal and third parties, have the same legal consequence as if it had been given to or obtained by the principal.

Illustrations

- (a) A is employed by B to buy from C certain goods, of which C is the apparent owner, and buys them accordingly. In the course of the treaty for the sale, A learns that the goods really belonged to D, but B is ignorant of that fact. B is not entitled to set off a debt owing to him from C against the price of the goods.
- (b) A is employed by B to buy from C goods of which C is the apparent owner. A was, before he was so employed, a servant of C, and then learnt that the goods really belonged to D, but B is ignorant of that fact. In spite of the knowledge of his agent, B may set off against the price of the goods a debt owing to him from C.



AGENT CANNOT PERSONALLY ENFORCE, NOR BE BOUND BY, CONTRACTS ON BEHALF OF PRINCIPAL

In the absence of any contract to that effect, an agent cannot personally enforce contracts entered into by him on behalf of his principal, nor is he personally bound by them.

Presumption of contract to the contrary—Such a contract shall be presumed to exist in the following cases :

- (1) Where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad;
- (2) Where the agent does not disclose the name of his principal; and
- (3) Where the principal, though disclosed, cannot be sued.

RIGHTS OF PARTIES TO A CONTRACT MADE BY AGENT NOT DISCLOSED

If an agent makes a contract with a person who neither knows, nor has reason to suspect, that he is an agent, his principal may require the performance of the contract; but the other contracting party has, as against the principal, the same right as he would have had as against the agent if the agent had been the principal.

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 a principal, he would not have entered into the contract.

PERFORMANCE OF CONTRACT WITH AGENT SUPPOSED TO BE PRINCIPAL

Where one man makes a contract with another, neither knowing nor having reasonable ground to suspect that the other is an agent, the principal, if he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract.

Illustration

A, who owes 500 rupees to B, sells 1,000 rupees worth of rice to B. A is acting as agent for C in the transaction, but B has no knowledge nor reasonable ground of suspicion that such is the case. C cannot compel B to take the rice without allowing him to set off A's debt.

RIGHT OF PERSON DEALING WITH AGENT PERSONALLY LIABLE

In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them, liable.

Illustration

A enters into a contract with B to sell him 100 bales of cotton, and afterwards discovers that B was acting as agent for C. A may sue either B or C, or both, for the price of the cotton.

CONSEQUENCE OF INDUCING AGENT OR PRINCIPAL TO ACT ON BELIEF THAT PRINCIPAL OR AGENT WILL BE HELD EXCLUSIVELY LIABLE

When a person who has made a contract with an agent induces the agent to act upon the belief that the principal only will be held liable, or induces the principal to act upon the belief that the agent only will be held liable, he cannot afterwards hold liable the agent or principal respectively.

LIABILITY OF PRETENDED AGENT

A person untruly representing himself to be the authorised agent of another, and thereby inducing a third person to deal with him as such agent, is liable, if his alleged employer does not ratify his acts, to make compensation to the other in respect of any loss or damage which he has incurred by so dealing.

PERSON FALSELY CONTRACTING AS AGENT NOT ENTITLED TO PERFORMANCE

A person with whom a contract has been entered into in the character of agent, is not entitled to require the performance of it if he was in reality acting, not as agent, but on his own account.

**LIABILITY OF PRINCIPAL INDUCING BELIEF THAT AGENT'S UNAUTHORIZED ACTS WERE AUTHORIZED**

When an agent has, without authority, done acts or incurred obligations to third persons on behalf of his principal, the principal is bound by such acts or obligations, if he has by his words or conduct induced such third persons to believe that such acts and obligations were within the scope of the agent's authority.

Illustrations

- (a) A consigns goods to B for sale, and gives him instructions not to sell under a fixed price. C, being ignorant of B's instructions, enters into a contract with B to buy the goods at a price lower than the reserved price. A is bound by the contract.
- (b) A entrusts B with negotiable instruments endorsed in blank. B sells them to C in violation of private orders from A. The sale is good.

EFFECT, ON AGREEMENT, OF MISREPRESENTATION OR FRAUD BY AGENT

Misrepresentations made, or frauds committed, by agents acting in the course of their business for their principals, have the same effect on agreements made by such agents as if such misrepresentations or frauds had been made, or committed, by the principals; but misrepresentations made, or frauds committed, by agents, in matters which do not fall within their authority, do not affect their principals.

Illustrations

- (a) A, being B's agent for the sale of goods, induces C to buy them by a misrepresentation, which he was not authorized by B to make. The contract is voidable, as between B and C, at the option of C.
- (b) A, the captain of B's ship, signs bills of lading without having received on board the goods mentioned therein. The bills of lading are void as between B and the pretended consignor.

IRREVOCABLE AGENCY

An agency is irrevocable in the following circumstances:

- (i) Where agency is coupled with interest for the agent over and above his remuneration.
- (ii) Where the agent has incurred personal liability.
- (iii) Where the agent has already exercised a part of his authority, so far as acts already done.



Study Note – 2

SALE OF GOODS ACT, 1930

This study note includes

- Sales of Goods Act' 1930 - Concepts and Definitions
- Condition and Warranty
- Passing of the Property from the Seller to the Buyer
- Performance of the Contract of Sale
- Rights of an Unpaid Seller
- Breach of Contract to deliver Specific or Ascertained Goods

2.1. SALES OF GOODS ACT, 1930 - CONCEPTS AND DEFINITIONS

2.1.1 INTRODUCTION

In trade and commerce, sales and purchase of goods are very common transactions. These transactions may appear to be very simple but the possibilities of complications is always there. Therefore knowledge of basic principles of sale and purchase is very much essential for all the concerned parties as well as for the entire community.

The Sale of Goods Act contains the basic principles as well as the legal framework of transactions of sale and purchase.

Earlier the Sale of Goods Act was a part of the Indian Contract Act. A separate Act was framed in the year 1930

EXTENT

It extends to the whole of India (except the State of Jammu and Kashmir).

It shall come into force on the 1st day of July, 1930.

2.1.2 BASIC CONCEPTS

- (1) 'Buyer' means a person, who buys or agrees to buy goods,
- (2) "Delivery" means voluntary transfer of possession from one person to another.
- (3) "Sale" means transfer of property in goods for a price.
- (4) "Hire – Purchase Agreement" means the seller delivers the possession of the goods to the other person and he charges rent for the goods. After receiving the price of the goods, the ownership of the goods is passed on to the purchaser
- (5) "Barter exchange" means exchange of goods for goods.
- (6) "Bailment" means only the possession is transferred from the bailor to the bai lee. Such transactions may be for the purpose of keeping the goods in the safe custody or may be for furnishing security.

2.1.3 Definition of Sale

Section 4 defines 'sale' as :

A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price.



- (1) A contract of sale is made by an offer to buy or sell goods for a price and the acceptance of such offer. The contract may provide for the immediate delivery of the goods or immediate payment of the price or both, or for the delivery or payment by installments, or that the delivery or payment or both shall be postponed.
- (2) Subject to the provisions of any law for the time being in force, a contract of sale may be made in writing or by word of mouth, or partly in writing and partly by word of mouth or may be implied from the conduct of the parties.

2.1.4 Essential of a Contract of Sale

- (1) There must be at least two parties as a person cannot sell goods to himself. However there may be a contract of sale between one part-owner and another.
- (2) There must be a transfer or agreement to transfer the **ownership** of goods from one person to another. Mere transfer of possession is not sale.
- (3) The subject matter of sale must be 'goods' and movable. The transfer of immovable property is not governed by Sale of Goods Act, 1930.
- (4) The consideration for sale is called price which should be stated in terms of 'money'. Exchange of 'goods' for 'goods' is barter and not sale. However price may be paid partly in terms of money and partly in kind.
- (5) All essential elements of a valid contract must be present in a contract of sale.
- (6) A contract of sale may be absolute or conditional.

2.1.5 Difference between sale and agreement to sale

Sale	Agreement to Sale
1. Sale is an executed contract. Property in the goods passes from seller to buyer.	It is an executory contract. Transfer of property in goods is to take place at a future date subject to fulfillment of certain conditions.
2. If goods are destroyed, the loss will be borne by the buyer even though they may be in possession of the seller.	The loss will be borne by the seller even though the goods may be in possession of the buyer.
3. A sale gives right to the buyer to enjoy the goods against the whole world including the seller.	The buyer only can sue the seller for damages.
4. In case of sale, the buyer can be sued for price of goods.	The buyer can be sued only for damages.
5. If buyer becomes insolvent before payment is made, the seller has to deliver the goods to the official receiver unless he has lien on them.	Seller may refuse to deliver the goods to the official receiver.
6. If the seller becomes insolvent after payment of price, the buyer can claim the goods from the official receiver.	The buyer cannot claim the goods. He can only claim ratable dividend for the amount paid by him.
7. The seller cannot resale the goods.	In this case, if the subsequent buyer takes in good faith and for consideration, he gets a good title. The original buyer may only sue the seller for damages.

2.1.6 Classification of goods

The goods which form the subject of a contract of sale may be either existing goods, owned or possessed by the seller, or future goods [Sec 6(1)] or contingent goods [Sec 6(2)].



1. Existing goods are owned by the seller at the time of sale. They are of the following types:
 - (i) Specific goods –These are identified and agreed upon at the time of sale.
 - (ii) Ascertained goods- These become ascertained after the contract is made.
 - (iii) Generic goods-These are not ascertained at the time of contract and is defined only by description.
2. Future goods are not owned by the seller at the time of contract but manufactured or acquired by him subsequent to formation of contract. Where by a contract of sale the seller purports to effect a present sale of future goods , the contract operates as an agreement to sale.
3. Contingent goods –These are goods the acquisition of which by seller depends upon a contingency which may or may not happen.

2.1.7 Effect of Destruction of Goods [Sec 7]

Goods perishing before making of contract (Sec 7) – Where there is a contract for the sale of specific goods, the contract is void if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description in the contract.

Goods perishing before sale but after agreement to sell (Sec 8) – Where there is an agreement to sell specific goods, and subsequently the goods without any fault on the part of the seller or buyer perish or become so damaged as no longer to answer to their description in the agreement before the risk passes to the buyer, the agreement is thereby avoided.

Sec (7 & 8) are applicable only in case of specific goods and not uncertained/generic goods.

2.1.8 Price

(Secs. 9 & 10) In a contract of sale ‘price’ to the consideration for sale of goods and is expressed in terms of money. It forms essential part of contract.

Ascertainment of Price

- (1) The price in a contract of sale may be fixed by the contract or may be left to be fixed in manner thereby agreed or may be determined by the course of dealing between the parties.
- (2) Where the price is not determined in accordance with the foregoing provisions, the buyer shall pay the seller a reasonable price. What is a reasonable price is a question of fact dependent on the circumstances of each particular case.

2.1.9 Document of title of goods

It symbolizes the goods and confers a right to the owner to take possession of the same or further transfer the right to some other person. A delivery order , railway receipt, bill of lading are some of the examples of document of title to goods.

2.1.10 Agreement to sell at valuation

- (1) Where there is an agreement to sell goods on the terms that the price is to be fixed by the valuation of a third party and such third party cannot or does not make such valuation, the agreement is thereby avoided :

Provided that, if the goods or any part thereof have been delivered to, and appropriated by, the buyer, he shall pay a reasonable price therefor.

- (2) Where such third party is prevented from making the valuation by the fault of the seller or buyer, the party not in fault may maintain a suit for damages against the party in fault.

2.1.11 Stipulations as to time (Sec 11)

Unless a different intention appears from the terms of the contract, stipulations as to time of payment are not deemed to be of the essence of a contract of sale. Whether any other stipulation as to time is of the essence of the contract or not depends on the terms of the contract.



2.2. CONDITION AND WARRANTY

2.2.1 INTRODUCTION

It is quite customary in a contract of sale that the seller makes certain statements to influence the buyer and motivate him to buy the goods. The question which arises here is that whether the statements made by the seller forms the part of the contract of sale or not?

If they do form the part of the contract and if there is a difference between the actual goods and the goods described in the statement, whether the buyer can treat that as a breach of contract?

2.2.2 CONDITION AND WARRANTY

Definitions

- (1) A stipulation in a contract of sale with reference to goods which are the subject thereof may be a condition or a warranty.
- (2) As per Sec 12(2) of the sale of Goods Act, a condition is a stipulation essential to the main purpose of the contract, the breach of which gives rise to right to treat the contract as repudiated.
- (3) As per Sec 12(3) of the sale of Goods Act, a warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated.
- (4) Whether a stipulation in a contract of sale is condition or a warranty depends in each case on the construction of the contract, a stipulation may be a condition though called warranty in a contract. [Sec 12(4)]

2.2.3 When condition to be treated as warranty

- (1) Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the condition as a breach of warranty and not as a ground for relating the contract as repudiated.
- (2) Where a contract of sale is not severable and the buyer has accepted the goods or part thereof, the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a term of the contract, express or implied, to that effect.
- (3) Nothing in this section shall affect the case of any condition or warranty fulfillment of which is excused by law by reason of impossibility or otherwise.

2.2.4 Conditions and Warranties may be either expressed or implied

When terms of contract expressly provide for them, they are known as express conditions or warranties. Implied conditions and warranties are incorporated in every contract of sale unless the circumstances show a different intention.

Implied conditions are of the following types :

(i) Condition as to title [Sec 14(a)]

In a contract of sale, unless the circumstances of the contract are such as to show a different intention, there is—

- (a) An implied condition on the part of the seller that, in the case of a sale, he has a right to sell the goods and that, in the case of an agreement to sell, he will have a right to sell the goods at the time when the property is to pass.
- (b) An implied warranty that the buyer shall have and enjoy quiet possession of the goods.
- (c) An implied warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time when the contract is made.

(ii) Sale by description (Sec 15)

Where there is a contract for the sale of goods by description, there is an implied condition that the goods shall correspond with the description, and, if the sale is by sample as well as by description, it is not sufficient that the bulk of the goods corresponds with the sample if the goods do not also correspond with the description.



(iii) Condition as to quality or fitness (Sec 16)

As per Sec 16 of the Sale of Goods Act Subject to the provisions of this Act and of any other law for the time being in force, there is no implied warranty or condition as to the quality or fitness for any particular purpose of goods supplied under a contract of sale, excepts as follows:-

- (1) Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which the goods are required, so as to show that the buyer relies on the seller's skill or judgement, and the goods are of a description which it is in the course of the seller's business to supply (whether he is the manufacturer or producer or not), there is an implied condition that the goods shall be reasonably fit for such purpose :

Provided that, in the case of a contract for the sale of a specified article under its patent or other trade name, there is no implied conditions to its fitness for any particular purpose.

- (2) Where goods are bought by description from a seller who deals in goods of that description (whether he is the manufacturer or producer or not), there is an implied condition that the goods shall be of merchantable quality.

Provided that, if the buyer has examined the goods, there shall be no implied conditions as regards defects which such examination ought to have revealed.

- (3) An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade.
- (4) An express warranty or conditions does not negative a warranty or condition implied by this Act unless inconsistent therewith.

(iv) Sale by sample (Sec 17)

- (1) A contract of sale is a contract for sale by sample where there is a term in the contract, express or implied, to that effect.
- (2) In the case of a contract for sale by sample there is an implied condition -
 - (a) That the bulk shall correspond with the sample in quality.
 - (b) That they shall have a reasonable opportunity of comparing the bulk with the sample.
 - (c) That the goods shall be free from any defect, rendering them un-merchantable, which would not be apparent on reasonable examination of the goods.

Implied warranties are of following types:

- (i) Warranty of quiet possession [Sec.14(b)] If the buyer in any way is disturbed from enjoying the quiet possession of goods purchased because of seller's defective title, the buyer can claim damages from seller.
- (ii) Warranty of freedom from encumbrances[Sec.14(c)]

The buyer is also entitled to additional warranty that the goods are free from any charge or right of any third party, not declared or known to the buyer.

2.2.5 Goods must be ascertained

Where there is a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are sanctioned.

Doctrine of Caveat Emptor – Caveat Emptor means 'let buyer be aware'. It is a fundamental principle of law of sale of goods and implies that the seller is under no obligation to point out the defects in his own goods. The doctrine is however subject to following exceptions:

- (i) In case of implied conditions and warranties.
- (ii) When the buyer makes it known to seller the purpose and depends on his expertise.
- (iii) When the seller commits fraud.
- (iv) When there is a usage of trade.



2.3. PASSING OF THE PROPERTY FROM THE SELLER TO THE BUYER

2.3.1. INTRODUCTION

A Sale is defined as transfer of ownership of the goods from the seller to the buyer for a price. Therefore what is important in a transaction of sale is the transfer of the ownership. It is essential to determine the exact point of time at which the ownership of the goods is transferred in favour of the buyer. Sections 18 to 25 of the Sale of Goods Act, determine when the property passes from the seller to the buyer.

(i) Goods must be ascertained

Where there is a contract for sale of unascertained goods, the property in the goods does not pass to the buyer till the goods are ascertained.

(ii) Intention of the parties for such transfer

- (1) Where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred.
- (2) For the purpose of ascertaining the intention of the parties regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case.

2.3.2.1 Specific goods

(i) Specific goods in a deliverable state

Where there is an unconditional contract for the sale of specific goods in a deliverable state, the property in the goods passes to the buyer when the contract is made, and it is immaterial whether the time of payment of the price or the time of delivery of the goods, or both, is postponed.

(ii) Specific goods to be put into a deliverable state

Where there is a contract for the sale of specific goods and the seller is bound to do something to the goods for the purpose of putting them into a deliverable state, the property does not pass until such thing is done and the buyer has notice thereof.

(iii) Specific goods in a deliverable state, when the seller has to do anything thereto in order to ascertain price

Where there is a contract for the sale of specific goods in a deliverable state, but the seller is bound to weigh, measure, test or do some other act or thing with reference to the goods for the purpose of ascertaining the price, the property does not pass until such act or thing is done and the buyer has notice thereof.

2.3.2.2 Unascertained goods

- (1) Where there is a contract for the sale of unascertained or future goods by description and goods of that description and in a deliverable state are unconditionally appropriated to the contract, either by the seller with the assent of the buyer or by the buyer with the assent of the seller, the property in the goods thereupon passes to the buyer. Such assent may be expressed or implied, and may be given either before or after the appropriation is made.
- (2) Delivery to carrier – Where, in pursuance of the contract, the seller delivers the goods.

2.3.2.3 Goods on approval or 'on sale or return'

When goods are delivered to the buyer on approval or on sale or return or other similar terms, the property therein passes to the buyer—

- (a) When he signifies his approval or acceptance to the seller to do not other act adopting the transaction.
- (b) If he does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection, then, if a time has been fixed for the return of the goods, on the expiration of such time, and, if not time has been fixed, on the expiration of a reasonable time.

2.3.3 Reservation of right of disposal

- (1) Where there is a contract for the sale of specific goods or where goods are subsequently appropriated to the contract, the seller may, by the terms of the contract or appropriation, reserve the right of disposal



of the goods until certain conditions are fulfilled. In such case, notwithstanding the delivery of the goods to a buyer, or to a carrier or other bailee for the purpose of transmission to the buyer, the property in the goods does not pass to the buyer until the conditions imposed by the seller are fulfilled.

- (2) Where goods are shipped or delivered to a railway administration for carriage by railway and by the bill of lading or railway receipt, as the case may be, the goods are deliverable to the order of the seller or his agent, the seller is prima facie deemed to reserve the right of disposal.
- (3) Where the seller of goods draws on the buyer for the price and transmits to the buyer the bill of exchange together with the bill of lading or, as the may be, the railway receipt, to secure acceptance to payment of the bill of exchange, the buyer is bound to return the bill of lading or the railway receipt if he does not honour the bill of exchange, and, if he wrongfully retains the bill of lading or the railway receipt, the property in the goods does not pass to him.

Explanation : In this section, the expression “railway” and “railway administration” shall have the meanings respectively assigned to them under the Indian Railways Act, 1890.

2.3.4 Risk prima facie passes with property

Unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer, but when the property therein is transferred to the buyer, the goods are at the buyer's risk whether delivery has been made or not.

2.3.5 Sale by person not the owner

Where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had, unless the owner of the goods is by conduct precluded from denying the seller's authority to sell.

However, this is subject to certain exceptions as follows :

- (i) **Sale by mercantile agent :** Where a mercantile agent is, with the consent of the owner, in possession of the goods or of a document of title to the goods, any sale made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same, provided that the buyer acts in good faith and has not at the time of the contract of sale notice that the seller has not authority to sell.
- (ii) **Sale by one of joint owners :** If one of several joint owners of goods has the sole possession of them by permission of the co-owners, the property in the goods is transferred to any person who buys them of such joint owner in good faith and has not at the time of the contract of sale notice that the seller has not authority to sell.
- (iii) **Sale by person in possession under voidable contract :** When the seller of goods has obtained possession thereof under a contract voidable under Section 19 or Section 19A of the Indian Contract Act, 1872, but the contract has not been rescinded at the time of the sale, the buyer acquires a good title to the goods, provided he buys them in good faith and without notice of the seller's defect of title.
- (iv) **Seller or buyer in possession after sale :**
 - (a) Where a person, having sold goods, continues or is in possession of the goods or of the documents of title to the goods, the delivery or transfer by that person or by a mercantile agent acting for him of the goods or documents of title under any sale, pledge or other disposition thereof to any person receiving the same in good faith and without notice of the previous sale shall have the same effect as if the person making the delivery or transfer were expressly authorised by the owner of the goods to make the same.
 - (b) Where a person, having bought or agreed to buy goods, obtains with the consent of the seller, possession of the goods or the documents of title to the goods, the delivery or transfer by that person or by a mercantile agent acting for him, of the goods or documents of title under any sale, pledge or other disposition thereof to any person receiving the same in good faith and without notice of any lien or other right of the original seller in respect of the goods shall have effect as if such lien or right did not exist.



- (v) **Sale by estoppel** : Where the owner by his conduct or omission, leads the buyer to believe that the seller has authority to sell, he is estopped from denying the fact afterwards. The buyer thus gets a better title than the seller.

For example A tells B in presence of C that A is agent of C. C maintains silence instead of denying it. Later if A sells C's goods to B, C cannot dispute B's title to the goods.

- (vi) Sale by an unpaid seller after exercising his right of lien or stoppage in transit.
- (vii) **Exceptions in other Acts:**
- (a) Sale by Official Receiver or Liquidator.
 - (b) Sale by a pawnee or pledgee in certain cases.
 - (c) Sale by finder of lost goods in certain cases.

2.3.6 Duties of seller and buyer

It is the duty of the seller to deliver the goods and of the buyer to accept and pay for them, in accordance with the terms of the contract of sale.

2.4. PERFORMANCE OF THE CONTRACT OF SALE

2.4.1 Introduction

Performance of a Contract of sale means as regards the Seller, delivery of goods to the buyer. From buyer's side the performance means the acceptance of the delivery of goods and payment for them as per the terms and conditions of sale.

2.4.2 Payment and delivery

Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions, that is to say, the seller shall be ready and willing to give possession of the goods to the buyer in exchange for the price, and the buyer shall be ready and willing to pay the price in exchange for possession of the goods.

2.4.3 Delivery

As per the Sale of Goods Act, Delivery is defined as the voluntary transfer of possession from one person to another.

Delivery of goods sold may be made by doing anything which the parties agree shall be treated as delivery or which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf.

Rules as to delivery :

(1) Delivery of goods and payment of price are concurrent conditions unless otherwise agreed upon.

(2) Effect of part delivery

A delivery of part of goods, in progress of the delivery of the whole has the same effect, for the purpose of passing the property in such goods, as a delivery of the whole, but a delivery of part of the goods, with an intention of severing it from the whole, does not operate as a delivery of the remainder.

(3) Buyer to apply for delivery

Apart from any express contract, the seller of goods is not bound to deliver them until the buyer applies for delivery.

(4) Place of delivery

Whether it is for the buyer to take possession of the goods or for the seller to send them to the buyer is a question depending in each case on the contract, express or implied, between the parties. Apart from any such contract, goods sold are to be delivered at the place at which they are at the time of the sale, and goods agreed to be sold are to be delivered at the place at which they are at the time of the agreement to sell, if not then in existence, at the place at which they are manufactured or produced.



(5) Time of delivery

Where under the contract of sale the seller is bound to send the goods to the buyer, but no time for sending them is fixed, the seller is bound to send them within a reasonable time.

Demand or tender of delivery may be treated as ineffectual unless made at a reasonable hour. What is a reasonable hour is a question of fact.

(6) Goods in possession of a third person

Where the goods at the time of sale are in the possession of a third person, there is no delivery by seller to buyer unless and until such third person acknowledges to the buyer that he holds the goods on his behalf.

(7) Cost of delivery

Unless otherwise agreed, the expense of and incidental to putting the goods into a deliverable state shall be borne by the seller.

(8) Mode of delivery

Delivery of goods may be actual, symbolic or constructive.

(9) Delivery of wrong quality

- (1) Where the seller delivers to the buyer a quantity of good less than he contracted to sell, the buyer may reject them, but if the buyer accepts the goods so delivered he shall pay for them at the contract rate.
- (2) Where the seller delivers to the buyer a quantity of goods larger than he contracted to sell the buyer may accept the goods included in the contract and reject the rest, or he may reject the whole. If the buyer accepts the whole of the goods so delivered, he shall pay for them at the contract rate.
- (3) Where the seller delivers to the buyer the goods he contract to sell mixed with goods of a different description not included in the contract, the buyer may accept the goods which are in accordance with the contract and reject the rest, or may reject the whole.
- (4) The provisions of this section are subject to any usage of trade, special agreement or course of dealing between the parties.

(10) Installment delivery

- (1) Unless otherwise agreed, the buyer of goods is not bound to accept delivery thereof by installments.
- (2) Where there is a contract for the sale of goods to be delivered by stated installments which are to be separately paid for, and the seller makes no delivery or defective delivery in respect of one or more installments, or the buyer neglects or refuses to take delivery of or pay for one or more installments, it is a question in each case depending on the terms of the contract and the circumstances of the case, whether the breach of contract is a repudiation of the whole contract, or whether it is a severable breach giving rise to a claim for compensation, but not a right to treat the whole contract as repudiated.

(11) Delivery to carrier or wharfinger

- (1) Where, in pursuance of a contract of sale, the seller is authorised or required to send the goods to the buyer, delivery of the goods to a carrier, whether named by the buyer or not, for the purpose of transmission to the buyer, or delivery of the goods to a wharfinger for safe custody, is prima facie deemed to be a delivery of the goods to the buyer.
- (2) Unless otherwise authorised by the buyer, the seller shall make such contract with the carrier or wharfinger on behalf of the buyer as may be reasonable having regard to the nature of the goods and the other circumstances of the case. If the seller omits so to do, and the goods are lost or damaged in course of transit or whilst in the custody of the wharfinger, the buyer may decline to treat the delivery to the carrier or wharfinger as a delivery to himself, or may hold the seller responsible in damages.
- (3) Unless otherwise agreed, where goods are sent by the seller to the buyer by a route involving sea transit, in circumstances in which it is usual to insure, the seller shall give such notice to the buyer as may enable him to insure them during their sea transit and if the seller fails so to do, the goods shall be deemed to be at his risk during such sea transit.

(12) Risk where goods are delivered at distant place

Where the seller of goods agrees to deliver them at his own risk at place other than that where they are when



sold, the buyer shall, nevertheless, unless otherwise agreed, take any risk of deterioration in the goods necessarily incident to the course of transit.

(13) Buyer's right of examination the goods

- (1) Where goods are delivered to the buyer which he has not previously examined, he is not deemed to have accepted them unless and until he has a reasonable opportunity of examining them for the purpose of ascertaining whether they are in conformity with the contract.
- (2) Unless otherwise agreed, when the seller tenders delivery of goods to the buyer, he is bound, on request, to afford the buyer a reasonable opportunity of examining the goods for the purpose of ascertaining whether they are in conformity with the contract.

(14) Buyer not bound to return rejected goods

Unless otherwise agreed, where goods are delivered to the buyer and he refuses to accept them, having the right so to do, he is not bound to return them to the seller, but it is sufficient if he intimates to the seller that he refuses to accept them.

(15) Liability of buyer for neglecting or refusing delivery of goods

When the seller is ready and willing to deliver the goods and requests the buyer to take delivery, and the buyer does not within a reasonable time after such request take delivery of the goods, he is liable to the seller for any loss occasioned by his neglect or refusal to take delivery and also for a reasonable charge for the care and custody of the goods.

Nothing in this section shall affect the rights of the seller where the neglect or refusal of the buyer to take delivery amounts to a repudiation of the contract :

Delivery are of following types:

Actual- In this case goods are handed over by the seller to the buyer or his authorized agent.

Symbolic- When goods are bulky and actual delivery is not possible, the delivery may be symbolic ,e.g. handing over the keys of the godown.

Constructive- This happens in the ways mentioned below:

- (i) When seller holding the possession of goods, agrees to hold them on behalf of the buyer.
- (ii) When buyer holding the possession of goods, with seller's consent, holds them as owner.
- (iii) When a third person holding the possession of goods on behalf of seller, acknowledges to hold them on behalf buyer.

2.5. RIGHTS OF AN UNPAID SELLER**INTRODUCTION**

In a transaction of sale it is not possible to avoid credit sales. In credit sales there is a risk of a debtor not paying the price of the goods even after the credit period is over. The seller of the goods therefore must possess some rights which he can use to secure payment of the price. If the recovery of the price is not possible due to the reason of bankruptcy of the buyer, he must have some other remedies. The Sale of Goods Act has made elaborate provisions regarding the rights of an unpaid seller.

“UNPAID SELLER”

- (1) The seller of goods is an “unpaid seller” -
 - (a) When the whole of the price has not been paid or tendered.
 - (b) When a bill of exchange or other negotiable instrument has been received as conditional payment and the conditions on which it was received has not been fulfilled by reason of the dishonour of the instrument or otherwise.



- (2) The term “seller” includes any person who is in the position of a seller, as, for instance, an agent of the seller to whom the bill of lading has been endorsed, or a consignor or agent who has himself paid, or is directly responsible for, the price.

Illustrations

- (a) Z sells goods worth Rs. 50,000/- to B on credit of 5 months. After 5 months B did not pay the price. Z shall be regarded as an unpaid seller.
- (b) In the above example if B accepts a bill of exchange and it is dishonoured by him on due date, A shall be considered as an unpaid seller.

UNPAID SELLER'S RIGHTS

An unpaid seller has the following rights by implication of law. These rights can easily be classified in the following categories -

I. RIGHT AGAINST GOODS

- (a) Right of lien; a lien on the goods for the period while he is in possession of them,
- (b) Right of stoppage in transit; In case of the insolvency of the buyer a right of stopping the goods in transit after he has parted with the possession of them,
- (c) Right of re-sale .
2. Where the property in goods has not passed to the buyer, the unpaid seller has, in addition to his other remedies, a right of withholding delivery similar to and co-extensive with his rights of lien and stoppage in transit where the property has passed to the buyer.

(a) RIGHT OF LIEN (SELLER'S LIEN)

- (1) The unpaid seller of goods who is in possession of them is entitled to retain possession of them until payment or tender of the price in the following cases, namely -
- (a) Where the goods have been sold without any stipulations as to credit,
- (b) Where the goods have been sold on credit, but the term of credit has expired,
- (c) Where the buyer becomes insolvent,
- (2) The seller may exercise his right of lien notwithstanding that he is in possession of the goods as agent or bailee for the buyer.

PART DELIVERY

Where an unpaid seller has made part delivery of the goods, he may exercise his right of lien on the remainder, unless such part delivery has been made under such circumstances as to show an agreement to waive the lien.

TERMINATION OF LIEN

- (1) The unpaid seller of goods loses his lien thereon—
- (a) When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods,
- (b) When the buyer or his agent lawfully obtains possession of the goods,
- (c) By waiver thereof.
- (2) The unpaid seller of goods, having a lien thereon, not lose his lien by reason only that he has obtained a decree for the price of the goods.

(b) RIGHT OF STOPPAGE IN TRANSIT

When the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit, that is to say, he may resume possession of the goods as long as they are in the course of transit, and may retain them until payment or tender of the price.

**DURATION OF TRANSIT**

- (1) Goods are deemed to be in course of transit from the time when they are delivered to a carrier or other bailee for the purpose of transmission to the buyer, until the buyer or his agent in that behalf takes delivery of them from such carrier or other bailee.
- (2) If the buyer or his agent in that behalf obtains delivery of the goods before their arrival at the appointed destination, the transit is at an end.
- (3) If, after the arrival of the goods at the appointed destination, the carrier or other bailee acknowledges to the buyer or his agent that he holds the goods on his behalf and continues in possession of them as bailee for the buyer or his agent, the transit is at an end and it is immaterial that a further destination for the goods may have been indicated by the buyer.
- (4) If the goods are rejected by the buyer and the carrier or other bailee continues in possession of them, the transit is not deemed to be at an end, even if the seller has refused to receive them back.
- (5) When goods are delivered to a ship chartered by the buyer, it is a question depending on the circumstances of the particular case, whether they are in the possession of the master as a carrier or as agent of the buyer.
- (6) Where the carrier or other bailee wrongfully refuses to deliver the goods to the buyer or his agent in that behalf, the transit is deemed to be at an end.
- (7) Where part delivery of the goods has been made to the buyer or his agent in that behalf, the remainder of the goods may be stopped in transit, unless such part delivery has been given in such circumstances as to show an agreement to give up possession of the whole of the goods.

HOW STOPPAGE IN TRANSIT IS EFFECTED

- (1) The unpaid seller may exercise his right to stoppage in transit either by taking actual possession of the goods, or by giving notice of his claim to the carrier or other bailee in whose possession the goods are. Such notice may be given either to the person in actual possession of the goods or to his principal. In the later case the notice, to be effectual, shall be given at such time and in such circumstances, that the principal, by the exercise of reasonable diligence, may communicate it to his servant or agent in time to prevent a delivery to the buyer.
- (2) Whether notice of stoppage in transit is given by the seller to the carrier or other bailee in possession of the goods, he shall re-deliver the goods to, or according to the directions of, the seller. The expenses of such re-delivery shall be borne by the seller.

EFFECT TO SUB-SALE OR PLEDGE BY BUYER

- (1) Subject to the provisions of this Act, the unpaid seller's right of lien or stoppage in transit is not affected by any sale or other disposition of the goods which the buyer may have made, unless the seller has assented thereto.

Provided that where a document of title to goods has been issued or lawfully transferred to any person as buyer or owner of the goods, and that person transfers the document to a person who takes the document in good faith and for consideration, then, if such last mentioned transfer was by way of sale, the unpaid seller's right of lien or stoppage in transit is defeated, and, if such last mentioned transfer was by way of pledge or other disposition for value, the unpaid seller's right of lien or stoppage in transit can only be exercised subject to the rights of the transferee.

- (2) Where the transfer is by way of pledge, the unpaid seller may require the pledgee to have the amount secured by the pledge satisfied in the first instance, as far as possible, out of any other goods or securities of the buyer in the hands of the pledgee and available against the buyer.

(c) RIGHT OF RE-SALE

- (1) A contract of sale is not rescinded by the mere exercise by an unpaid seller of his right of lien or stoppage in transit.
- (2) Where the goods are of a perishable nature, or where the unpaid seller who has exercised his right of lien or stoppage in transit gives notice to the buyer of his intentions to re-sell, the unpaid seller may, if the buyer does not within a reasonable time pay or tender the price, re-sell the goods within a reasonable



time and recover from the original buyer damages for any loss occasioned by his breach of contract, but the buyer shall not be entitled to any profit which may occur on the re-sale. If such notices are not given, the unpaid seller shall not be entitled to recover such damages and the buyer shall be entitled to the profit, if any, on the re-sale.

- (3) Where an unpaid seller who has exercised his right of lien or stoppage in transit re-sells the goods, the buyer acquires a good title thereto as against the original buyer, notwithstanding that no notice of the re-sale has been given to the original buyer.
- (4) Where the seller expressly reserves a right of re-sale in case the buyer should make default, and on, the buyer making default, re-sells the goods, the original contract of sale is thereby rescinded, but without prejudice to any claim which the seller may have for damages.

II. RIGHT AGAINST THE BUYER PERSONALLY

- (a) Suit for price.
- (b) Suit for damages for non-acceptance.
- (c) Repudiation of contract.
- (d) Suit for interest.

2.6. BREACH OF CONTRACT TO DELIVER SPECIFIC OR ASCERTAINED GOODS

INTRODUCTION

Subject to the provisions of Chapter II of the Specific Relief Act, 1877, in any suit for breach of contract to deliver specific or ascertained goods, the Court may, if it thinks fit, on the application of the plaintiff, by its decree direct that the contract shall be performed specifically, without giving the defendant the option of retaining the goods on payment of damages. The decree may be unconditional, or upon such terms and conditions as to damages, payment of the price or otherwise, as the Court may deem just, and the application of the plaintiff may be made at any time before the decree.

SUIT FOR PRICE

- (1) Where under a contract of sale the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract, the seller may sue him for the price of the goods.
- (2) Where under a contract of sale the price is payable on a day certain irrespective of delivery and the buyer wrongfully neglects or refuses to pay such price, the seller may sue him for the price although the property in the goods has not passed and the goods have not been appropriated to the contract

DAMAGES FOR NON-ACCEPTANCE

Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller may sue him for damages for non-acceptance

DAMAGES FOR NON-DELIVERY

Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may sue the seller for damages for non-delivery.

REMEDY FOR BREACH OF WARRANTY

- (1) Where there is a breach of warranty by the seller, or where the buyer elects or is compelled to treat any breach of a condition on the part of the seller as a breach of warranty, the buyer is not by reason only of such breach of warranty entitled to reject the goods; but he may-
 - (a) Set up against the seller the Breach of warranty in diminution or extinction of the price; or
 - (b) Sue the seller for damages for breach of warranty.
- (2) The fact that a buyer has set up a breach of warranty in diminution or extinction of the price does not prevent him from suing for the same breach of warranty if he has suffered further damage.

**REPUDIATION OF CONTRACT BEFORE DUE DATE**

Where either party to a contract of sale repudiates the contract before the date of delivery, the other may either treat the contracts as subsisting and wait till the date of delivery, or he may treat the contract as rescinded and use for damages for the breach.

INTEREST BY WAY OF DAMAGES AND SPECIAL DAMAGES

- (1) Nothing in this Act shall affect the right of the seller or the buyer to recover interest or special damages in any case whereby law interest or special damages may be recoverable, or to recover the money paid where the consideration for the payment of it has failed.
- (2) In the absence of a contract to the contrary, the Court may award interest at such rate as it think fit on the amount of the price—
 - (a) To the seller in a suit by him for the amount of the price.- from the date of the tender of the goods or from the date on which the price was payable.
 - (b) To the buyer in a suit by him for the refund of the price in a case of a breach of the contract on the part of the seller- from the date on which the payment was made.

AUCTION SALE

In the case of sale by auction—

- (1) Where goods are put up for sale in lots, each lot is prima facie deemed to be the subject of a separate contract of sale.
- (2) The sale is complete when the auctioneer announces its completion by the fall of the hammer or in other customary manner, and, until such announcement is made, any bidder may retract his bid.
- (3) A right to bid may be reserved expressly by or on behalf of the seller and, where such rights is expressly so reserved, but not otherwise, the seller or any one person on his behalf may, subject to the provisions hereinafter contained, bid at the auction,
- (4) Where the sale is not notified to be subject to a right to bid on behalf of the seller, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale, or for the auctioneer knowingly to take any bid from the seller or any such person, and any such person, and any sale contravening this rule may be treated as fraudulent by the buyer.
- (5) The sale may be notified to be subject to a reserved or upset price.
- (6) If the seller makes use of pretended bidding to raise the price, the sale is voidable at the option of the buyer.

TO SUM UP

- (1) Nothing in this Act or in any repeal affected thereby shall affect or be deemed to affect.
 - (a) Any right, title, interest, obligations or liability already acquired, accrued or incurred before the commencement of this Act, or
 - (b) Any legal proceedings or remedy in respect of any such right, title, interest, obligation or liability, or
 - (c) Anything done or suffered before the commencement of this Act, or
 - (d) Any enactment relating to the sale of goods which is not expressly repealed by this Act, or
 - (e) Any rule of law not inconsistent with this Act.
- (2) The rules of insolvency relating to contracts for the sale of goods shall continue to apply thereto, notwithstanding anything contained in this Act.
- (3) The provisions of this Act relating to contracts of sale do not apply to any transaction in the form of a contract of sale which is intended to operate by way of mortgage, pledge, charge or other security.



Study Note – 3

INDUSTRIAL LAWS

This study note includes

- The Factories Act, 1948
- Industrial Disputes Act, 1947
- Workmen Compensation Act, 1923
- Payment of Wages Act, 1936
- Minimum Wages Act, 1948
- Employees' Provident Funds and Miscellaneous Provisions Act, 1952
- Payment of Bonus Act, 1965
- Payment of Gratuity Act, 1972
- Consumer Protection Act, 1986

3.1 THE FACTORIES ACT 1948

INTRODUCTION

Extent and Commencement

- (1) This Act may be called the Factories Act, 1948.
- (2) It extends to the whole of India.
- (3) It shall come into force on the 1st day of April, 1949.

Basic Concepts

In this Act, unless there is anything repugnant in the subject or context, —

- (1) “Adult” means a person who has completed his eighteenth year of age;
- (2) “Adolescent” means a person who has completed his fifteen year of age but has not completed his eighteenth year;
- (3) “Calendar year” means the period of twelve months beginning with the first day of January in any year;
- (4) “Child” means a person who has not completed his fifteenth year of age;
- (5) “Competent person”, in relation to any provision of this Act, means a person or an institution recognised as such by the Chief Inspector for the purposes of carrying out tests, examinations and inspections required to be done in a factory under the provisions of this Act having regard to—
 - (i) The qualifications and experience of the person and facilities available at his disposal; or
 - (ii) The qualifications and experience of the persons employed in such institution and facilities available therein, with regard to the conduct of such test, examinations and inspections, and more than one person or institution can be recognised as a competent person in relation to a factory;
- (6) “Hazardous process” means any process or activity in relation to an industry specified to the First Schedule where, unless special care is taken, raw materials used therein or the intermediate or finished products, bye-products, wastes or effluents thereof would—
 - (i) Cause material impairment to the health of the persons engaged in or connected therewith, or



- (ii) Result in the pollution of the general environment : Provided that the State Government may, by notification in the Official Gazette, amend the First Schedule by way of addition, omission or variation of any industry specified in the said Schedule;
- (7) “Young person” means a person who is either a child or an adolescent;
- (8) “Day” means a period of twenty-four hours beginning at midnight;
- (9) “Week” means a period of seven days beginning at midnight on Saturday night or such other night as may be approved in writing for a particular area by the Chief Inspector of factories;
- (10) “Power” means electrical energy, or any other form of energy which is mechanically transmitted and is not generated by human or animal agency;
- (11) “Prime mover” means any engine, motor or other appliance which generates or otherwise provides power;
- (12) “Transmission machinery” means any shaft, wheel drum, pulley, system of pulleys, coupling, clutch, driving belt or other appliance or device by which the motion of a prime mover is transmitted to or received by any machinery or appliance;
- (13) “machinery” includes prime movers, transmission machinery and all other appliances whereby power is generated, transformed, transmitted or applied;
- (14) “Manufacturing process” means any process for—
- (i) Making, altering, repairing, ornamenting, finishing, packing, oiling, washing, cleaning, breaking up, demolishing, or otherwise treating or adapting any article or substance with a view to its use, sale, transport, delivery or disposal, or
 - (ii) Pumping oil, water, sewage or any other substance; or;
 - (iii) Generating, transforming or transmitting power; or
 - (iv) Composing types for printing, printing by letter press, lithography, photogravure or other similar process or book binding; lra-6] [lra-7 or lra-7]
 - (v) Constructing, reconstructing, repairing, refitting, finishing or breaking up ships or vessels; (Inserted by the Factories (Amendment) Act, 1976, w.e.f. 26-10-1976.)
 - (vi) Preserving or storing any article in cold storage;
- (15) “worker” means a person employed, directly or by or through any agency (including a contractor) with or without the knowledge of the principal employer, whether for remuneration or not, in any manufacturing process, or in cleaning any part of the machinery or premises used for a manufacturing process, or in any other kind of work incidental to, or connected with, the manufacturing process, or the subject of the manufacturing process but does not include any member of the armed forces of the union;
- (16) “Factory” means any premises including the precincts thereof –
- (i) Whereon ten or more workers are working, or were working on any day of the preceding twelve months, and in any part of which a manufacturing process is being carried on with the aid of power, or is ordinarily so carried on, or
 - (ii) Whereon twenty or more workers are working, or were working on any day of the preceding twelve months, and in any part of which a manufacturing process is being carried on without the aid of power, or is ordinarily so carried on, but does not include a mine subject to the operation of the Mines Act, 1952 (35 of 1952), or a mobile unit belonging to the armed forces of the union, a railway running shed or a hotel, restaurant or eating place;

Explanation I : For computing the number of workers for the purposes of this clause all the workers in different groups and relays in a day shall be taken into account.

Explanation II : For the purposes of this clause, the mere fact that an Electronic Data Processing Unit or a Computer Unit is installed in any premises or part thereof, shall not be construed to make it a factory if no manufacturing process is being carried on in such premises or part thereof;



Explanation II : ‘Precincts’ means a space enclosed by walls. What will come under precincts of a particular premises will depend on the circumstances of each case.

(17) “Occupier” of a factory means the person who has ultimate control over the affairs of the factory :

Provided that -

- (i) In the case of a firm or other association of individuals, any one of the individual partners or members thereof shall be deemed to be the occupier;
- (ii) In the case of a company, any one of the directors shall be deemed to be the occupier;
- (iii) In the case of a factory owned or controlled by the Central Government or any State Government, or any local authority, the person or persons appointed to manage the affairs of the factory by the Central Government, the State Government or the local authority, as the case may be, shall be deemed to be the occupier :

Provided further that in the case of a ship which is being repaired, or on which maintenance work is being carried out, in a dry dock which is available for hire, - (1) the owner of the dock shall be deemed to be the occupier for the purposes of any matter provided for by or under—

- (a) section 6, section 7, section 7A, section 7B, section 11 or section 12;
 - (b) Section 17, in so far as it relates to the providing and maintenance of sufficient and suitable lighting in or around the dock;
 - (c) Section 18, section 19, section 42, section 46, section 47 or section 49, in relation to the workers employed on such repair or maintenance;
- (2) The owner of the ship or his agent or master or other officer-in-charge of the ship or any person who contracts with such owner, agent or master or other officer-in-charge to carry out the repair or maintenance work shall be deemed to be the occupier for the purposes of any matter provided for by or under section 13, section 14, section 16 or section 17 (save as otherwise provided in this proviso) or Chapter IV (except section 27) or section 43, section 44 or section 45, Chapter VI, Chapter VII, Chapter VIII or Chapter IX or section 108, section 109 or section 110, in relation to—
- (a) The workers employed directly by him, or by or through any agency; and
 - (b) The machinery, plant or premises in use for the purpose of carrying out such repair or maintenance work by such owner, agent, master or other officer-in-charge or person;
- (18) Shift means where work of the same kind is carried out by two or more sets of workers working during different periods of the day, each of such sets is called a “group” or “relay” and each of such periods is called a “shift”.

REFERENCES TO TIME OF DAY

In this Act references to time of day are references to Indian Standard Time, being five and a half hours ahead of Greenwich Mean Time : Provided that for any area in which Indian Standard Time is not ordinarily observed the State Government may make rules—

- (a) Specifying the area,
- (b) Defining the local mean time ordinarily observed therein, and
- (c) Permitting such time to be observed in all or any of the factories situated in the area.

POWER TO DECLARE DIFFERENT DEPARTMENTS TO BE SEPARATE FACTORIES OR TWO OR MORE FACTORIES TO BE A SINGLE FACTORY

The State Government may, on its own or on an application made in this behalf by an occupier, direct, by an order in writing, and subject to such conditions as it may deem fit, that for all or any of the purposes of this Act different departments or branches of a factory of the occupier specified in the application shall be treated as separate factories or that two or more factories of the occupier specified in the application shall be treated as a single factory :

Provided that no order under this section shall be made by the State Government on its own motion unless an opportunity of being heard is given to the occupier.

**POWER TO EXEMPT DURING PUBLIC EMERGENCY**

In any case of public emergency the State Government may, by notification in the Official Gazette, exempt any factory or class or description of factories from all or any of the provisions of this Act except section 67 for such period and subject to such conditions as it may think fit : Provided that no such notification shall be made for a period exceeding three months at a time.

Explanation : For the purposes of this section “public emergency” means a grave emergency whereby the security of India or of any part of the territory thereof is threatened, whether by war or external aggression or internal disturbance.

APPROVAL, LICENSING AND REGISTRATION OF FACTORIES

- (1) The State Government may make rules - (a) requiring, for the purposes of this Act, the submission of plans of any class or description of factories to the Chief Inspector or the State Government;
 - (a) Requiring, the previous permission in writing of the State Government or the Chief Inspector to be obtained for the site on which the factory is to be situated and for the construction or extension of any factory or class or description of factories;
 - (b) Requiring for the purpose of considering applications for such permission the submission of plans and specifications;
 - (c) Prescribing the nature of such plans and specifications and by whom they shall be certified;
 - (d) Requiring the registration and licensing of factories or any class or description of factories, and prescribing the fees payable for such registration and licensing and for the renewal of licences;
 - (e) Requiring that no licence shall be granted or renewed unless the notice specified in section 7 has been given.
- (2) If on an application for permission referred to in clause (aa) of sub-section (1) accompanied by the plans and specifications required by the rules made under clause (b) of that sub-section, sent to the State Government or Chief inspector by registered post, no order is communicated to the applicant within three months from the date on which it is so sent, the permission applied for in the said application shall be deemed to have been granted.
- (3) Where a State Government or a Chief Inspector refuses to grant permission to the site, construction or extension of a factory or to the registration and licensing of a factory, the applicant may within thirty days of the date of such refusal appeal to the Central Government if the decision appealed from was of the State Government and to the State Government in any other case.

Explanation : A factory shall not be deemed to be extended within the meaning of this section by reason only of the replacement of any plant or machinery, or within such limits as may be prescribed, of the addition of any plant or machinery if such replacement or addition does not reduce the minimum clear space required for safe working around the plant or machinery or adversely affect the environmental conditions from the evolution or emission of steam, heat or dust or fumes injurious to health.

NOTICE BY OCCUPIER

1. The occupier shall, at least fifteen days before he begins to occupy or use any premises as a factory, send to the Chief Inspector a written notice containing—
 - (a) The name and situation of the factory;
 - (b) The name and address of the occupier;
 - (c) The name and address of the owner of the premises or building (including the precincts thereof) referred to in section 93;
 - (d) The address to which communication relating to the factory may be sent;
 - (e) The nature of the manufacturing process—
 - (i) Carried on in the factory during the last twelve months in the case of factories in existence on the date of the commencement of this Act, and
 - (ii) To be carried on in the factory during the next twelve months in the case of all factories;



- (f) The total rated horse power installed or to be installed in the factory, which shall not include the rated horse power of any separate stand-by plant;
 - (g) The name of the manager of the factory for the purposes of this Act;
 - (h) The number of workers likely to be employed in the factory;
 - (i) The average number of workers per day employed during the last twelve months in the case of a factory in existence on the date of the commencement of this Act;
2. In respect of all establishments which come within the scope of the Act for the first time, the occupier shall send a written notice to the Chief Inspector containing the particulars specified in sub-section (1) within thirty days, from the date of the commencement of this Act.
 3. Before a factory engaged in a manufacturing process which is ordinarily carried on for less than one hundred and eighty working days in the year resumes working, the occupier shall send a written notice to the Chief Inspector containing the particulars specified in sub-section (1) At least thirty days before the date of the commencement of work.
 4. Whenever a new manager is appointed, the occupier shall send to the Inspector a written notice and to the Chief Inspector a copy thereof within seven days from the date on which such person takes over charge.
 5. During any period for which no person has been designated as manager of a factory or during which the person designated does not manage the factory, any person found acting as manager, or if no such person is found, the occupier himself, shall be deemed to be the manager of the factory for the purposes of this Act.

GENERAL DUTIES OF THE OCCUPIER

1. Every occupier shall ensure, so far as is reasonably practicable, the health, safety and welfare of all workers while they are at work in the factory.
2. Without prejudice to the generality of the provisions of sub-section (1), the matters to which such duty extends, shall include—
 - (a) the provision and maintenance of plant and systems of work in the factory that are safe and without risks to health;
 - (b) the arrangements in the factory for ensuring safety and absence of risks to health in connection with the use, handling, storage and transport of articles and substances;
 - (c) the provision of such information, instruction, training and supervision as are necessary to ensure the health and safety, of all workers at work;
 - (d) the maintenance of all places of work in the factory in a condition that is safe and without risks to health and the provision and maintenance of such means of access to, and egress from, such places as are safe and without such risks;
 - (e) the provision, maintenance or monitoring of such working environment in the factory for the workers that is safe, without risks to health and adequate as regards facilities and arrangements for their welfare at work.
3. Except in such cases as may be prescribed, every occupier shall prepare, and, as often as may be appropriate, revise, a written statement of his general policy with respect to the health and safety of the workers at work and the organisation and arrangements for the time being in force for carrying out that policy, and to bring the statement and any revision thereof to the notice of all the workers in such manner as may be prescribed.

GENERAL DUTIES OF MANUFACTURERS, ETC., AS REGARDS ARTICLES AND SUBSTANCES FOR USE IN FACTORIES (Sec 7-B) : Introduced by Amendment Act, 1987. The provisions are as follows :-

1. Every person who designs, manufactures, imports or supplies any article for use in any factory shall—
 - (a) ensure, so far as is reasonably practicable, that the article is so designed and constructed as to be safe and without risks to the health of the workers when properly used;



- (b) carry out or arrange for the carrying out of such tests and examination as may be considered necessary for the effective implementation of the provisions of clause (a);
 - (c) take such steps as may be necessary to ensure that adequate information will be available—
 - (i) in connection with the use of the article in any factory;
 - (ii) about the use for which it is designed and tested; and
 - (iii) about any conditions necessary to ensure that the article, when put to such use, will be safe, and without risks to the health of the workers : Provided that where an article is designed or manufactured outside India, it shall be obligatory on the part of the importer to see -
 - (a) that the article conforms to the same standards if such article is manufactured in India, or
 - (b) if the standards adopted in the country outside for the manufacture of such article is above the standards adopted in India, that the article conforms to such standards.
2. Every person, who undertakes to design or manufacture any article for use in any factory, may carry out or arrange for the carrying out of necessary research with a view to the discovery and, so far as is reasonably practicable, the elimination or minimization of any risks to the health or safety of the workers to which the design or article may give rise.
 3. Nothing contained in sub-sections (1) and (2) shall be construed to require a person to repeat the testing, examination or research which has been carried out otherwise than by him or at his instance in so far as it is reasonable for him to rely on the results thereof for the purposes of the said sub-sections.
 4. Any duty imposed on any person by sub-sections (1) and (2) shall extend only to things done in the course of business carried on by him and to matters within his control.
 5. Where a person designs, manufactures, imports or supplies an article on the basis of a written undertaking by the user of such article to take the steps specified in such undertaking to ensure, so far as is reasonably practicable, that the article will be safe and without risks to the health of the workers when properly used, the undertaking shall have the effect of relieving the person designing, manufacturing, importing or supplying the article from the duty imposed by clause (a) of sub-section (1) to such extent as is reasonable having regard to the terms of the undertaking.
 6. For the purposes of this section, an article is not to be regarded as properly used if it is used without regard to any information or advice relating to its use which has been made available by the person who has designed, manufactured, imported or supplied the article.

Explanation : For the purposes of this section, “article” shall include plant and machinery.

INSPECTORS

- (1) The State Government may, by notification in the Official Gazette, appoint such persons as possess the prescribed qualification to be Inspectors for the purposes of this Act and may assign to them such local limits as it may think fit.
- (2) The State Government may, by notification in the Official Gazette, appoint any person to be a Chief Inspector who shall, in addition to the powers conferred on a Chief Inspector under this Act, exercise the powers of an Inspector throughout the State.
- (3) The State Government may, by notification in the Official Gazette, appoint as many Additional Chief Inspectors, Joint Chief Inspectors and Deputy Chief Inspectors and as many other officers as it thinks fit to assist the Chief Inspector and to exercise such of the powers of the Chief Inspector as may be specified in such notification.
- (4) Every Additional Chief Inspector, Joint Chief Inspector, Deputy Chief Inspector and every other officer appointed under sub-section (2A) shall, in addition to the powers of a Chief Inspector specified in the notification by which he is appointed, exercise the powers of an Inspector throughout the State.
- (5) No person shall be appointed under sub-section (1), sub-section (2) sub-section (2A) [ra-38] or sub-section (5), or having been so appointed, shall continue to hold office, who is or becomes directly or indirectly interested in a factory or in any process or business carried on therein or in any patent or machinery connected therewith.
- (6) Every District Magistrate shall be an Inspector for his district.



- (7) The State Government may also, by notification as aforesaid, appoint such public officers as it thinks fit to be additional Inspectors for all or any of the purposes of this Act, within such local limits as it may assign to them respectively.
- (8) In any area where there are more Inspectors than one the State Government may, by notification as aforesaid, declare the powers, which such Inspectors shall respectively exercise and the Inspector to whom the prescribed notices are to be sent.
- (9) Every Chief Inspector, Additional Chief Inspector, Joint Chief Inspector, Deputy Chief Inspector, Inspector and every other officer appointed under this section shall be deemed to be a public servant within the meaning of the Indian Penal Code (45 of 1860), and shall be officially subordinate to such authority as the State Government may specify in this behalf.

POWERS OF INSPECTORS

Subject to any rules made in this behalf, an Inspector may, within the local limits for which he is appointed,—

- (a) Enter, with such assistants being persons in the service of the Government, or any local or other public authority, or with an expert as he thinks fit, any place which is used, or which he has reason to believe is used, as a factory;
- (b) Make examination of the premises, plant, machinery, article or substance;
- (c) Inquire into any accident or dangerous occurrence, whether resulting in bodily injury, disability or not, and take on the spot or otherwise statements of any person which he may consider necessary for such inquiry;
- (d) Require the production of any prescribed register or any other document relating to the factory;
- (e) Seize, or take copies of, any register, record or other document or any portion thereof, as he may consider necessary in respect of any offence under this Act, which he has reason to believe, has been committed;
- (f) Direct the occupier that any premises or any part thereof, or anything lying therein, shall be left undisturbed (whether generally or in particular respects) for so long as is necessary for the purpose of any examination under clause (b);
- (g) Take measurements and photographs and make such recordings as he considers necessary for the purpose of any examination under clause (b), taking with him any necessary instrument or equipment;
- (h) In case of any article or substance found in any premises, being an article or substance which appears to him as having caused or is likely to cause danger to the health or safety of the workers, direct it to be dismantled or subject it to any process or test (but not so as to damage or destroy it unless the same is, in the circumstances necessary, for carrying out the purposes of this Act), and take possession of any such article of substance or a part thereof, and detain it for so long as is necessary for such examination;
- (i) exercise such other powers as may be prescribed:

Provided that no person shall be compelled under this section to answer any question or give any evidence tending to incriminate himself.

CERTIFYING SURGEONS (Sec. 10)

- (1) The State Government may appoint qualified medical practitioners to be certifying surgeons for the purposes of this Act within such local limits or for such factory or class or description of factories as it may assign to them respectively.
- (2) A certifying surgeon may, with the approval of the State Government, authorize any qualified medical practitioner to exercise any of his powers under this Act for such period as the certifying surgeon may specify and subject to such conditions as the State Government may think fit to impose, and references in this Act to a certifying surgeon shall be deemed to include references to any qualified medical practitioner when so authorized.
- (3) No person shall be appointed to be, or authorized to exercise the powers of, a certifying surgeon, or having been so appointed or authorized, continue to exercise such powers, who is, or becomes the occupier of a factory or is or becomes directly or indirectly interested therein or in any process or business carried on therein or in any patent or machinery connected therewith or is otherwise in the employ of the factory :



Provided that the State Government may, by order in writing and subject to such conditions as may be specified in the order, exempt any person or class of persons from the provisions of this sub-section in respect of any factory or class or description of factories.

- (4) The certifying surgeon shall carry out such duties as may be prescribed in connection with—
 - (a) The examination and certification of young persons under this Act;
 - (b) The examination of persons engaged in factories in such dangerous occupations or processes as may be prescribed;
 - (c) The exercising of such medical supervision as may be prescribed for any factory or class or description of factories where—
 - (i) cases of illness have occurred which it is reasonable to believe are due to the nature of the manufacturing process carried on, or other conditions of work prevailing, therein;
 - (ii) By reason of any change in the manufacturing process carried on or in the substances used therein or by reason of the adoption of any new manufacturing process or of any new substance for use in a manufacturing process, there is a likelihood of injury to the health of workers employed in that manufacturing process;
 - (iii) Young persons are, or are about to be, employed in any work which is likely to cause injury to their health. Explanation : In this section “qualified medical practitioner” means a person holding a qualification granted by an authority specified in the Schedule to the Indian Medical Degrees Act, 1916 (7 of 1916) or in the Schedules to the Indian Medical Council Act, 1933 (27 of 1933).

HEALTH

Sec. 11 to 20 deals with provisions ensuring health, safety and welfare of workers.

I. CLEANLINESS

- (1) Every factory shall be **kept clean and free from effluvia** arising from any drain, privy or other, nuisance, and in particular—
 - (a) Accumulations of dirt and refuse shall be removed daily by sweeping or by any other effective method from the floors and benches of workrooms and from staircases and passages, and disposed of in a suitable manner;
 - (b) The floor of every workroom shall be cleaned at least once in every week by washing, using disinfectant, where necessary, or by some other effective method;
 - (c) Where a floor is liable to become wet in the course of any manufacturing process to such extent as is capable of being drained, effective means of drainage shall be provided and maintained;
 - (d) All inside walls and partitions, all ceilings or tops of rooms and all walls, sides and tops of passages and staircases shall—
 - (i) where they are painted otherwise than with washable water-paint or varnished, be repainted or revarnished least once in every period of five years;
 - (ii) where they are painted with washable water paint, be repainted with at least one coat of such paint at least once in every period of three years and washed at least once in every period of six months;
 - (iii) where they are painted or varnished or where they have smooth impervious surfaces, be cleaned at least once in every period of fourteen months by such method as may be prescribed;
 - (iv) in any other case, be kept whitewashed or colourwashed, and the whitewashing or colourwashing shall be carried out at least once in every period of fourteen months;
 - (e) all doors and window frames and other wooden or metallic frame work and shutters shall be kept painted or varnished and the painting or varnishing shall be carried out at least once in every period of five years;
 - (f) the dates on which the processes required by clause (d) are carried out shall be entered in the prescribed register.



- (2) If, in view of the nature of the operations carried on in a factory or class or **description of factories** or any part of a factory or class or description of factories, it is not possible for the occupier to comply with all or any of the provisions of sub-section (1), the State Government may by order exempt such factory or class or description of factories or part from any of the provisions of that sub-section and specify alternative methods for keeping the factory in a clean state.

II. DISPOSAL OF WASTES AND EFFLUENTS

- (1) Effective arrangements shall be made in every factory for the treatment of wastes and effluents due to the manufacturing process carried on therein, so as to render them innocuous, and for their disposal.
- (2) The State Government may make rules prescribing the arrangements to be made under sub-section (1) or requiring that the arrangements made in accordance with sub-section (1) shall be approved by such Authority as may be prescribed.

III. VENTILATION AND TEMPERATURE

- (1) Effective and suitable provision shall be made in every factory for securing and maintaining in every workroom—
 - (a) adequate ventilation by the circulation of fresh air, and
 - (b) such a temperature as will secure to workers therein reasonable conditions of comfort and prevent injury to health; and in particular,—
 - (i) walls and roofs shall be of such material and so designed that such temperature shall not be exceeded but kept as low as practicable;
 - (ii) where the nature of the work carried on in the factory involves, or is likely to involve, the production of excessively high temperatures such adequate measures as are practicable shall be taken to protect the workers therefrom, by separating the process which produces such temperatures from the workroom, by insulating the hot parts or by other effective means.
- (2) The State Government may prescribe a standard of adequate ventilation and reasonable temperature for any factory or class or description of factories or parts thereof and direct that [1ra-48 proper measuring instruments, at such places and in such position as may be specified, shall be provided and such records, as may be prescribed, shall be maintained;
- (3) If it appears to the Chief Inspector that excessively high temperatures in any factory can be reduced by the adoption of suitable measures, he may, without prejudice to the rules made under sub-section (2), serve on the occupier, an order in writing specifying the measures which, in his opinion, should be adopted, and requiring them to be carried out before a specified date.

IV. DUST AND FUME

- (1) In every factory in which, by reason of the manufacturing process carried on, there is given off any dust or fume or other impurity of such a nature and to such an extent as is likely to be injurious or offensive to the workers employed therein, or any dust in substantial quantities, effective measures shall be taken to prevent its inhalation and accumulation in any workroom, and if any exhaust appliance is necessary for this purpose, it shall be applied as near as possible to the point of origin of the dust, fume or other impurity, and such point shall be enclosed so far as possible.
- (2) In any factory no stationary internal combustion engine shall be operated unless the exhaust is conducted into the open air, and no other internal combustion engine shall be operated in any room unless effective measures have been taken to prevent such accumulation of fumes therefrom as are likely to be injurious to workers employed in the room.

V. ARTIFICIAL HUMIDIFICATION

- (1) In respect of all factories in which the humidity of the air is artificially increased, the State Government may make rules,—
 - (a) prescribing standards of humidification;
 - (b) regulating the methods used for artificially increasing the humidity of the air,



- (c) directing prescribed tests for determining the humidity of the air to be correctly carried out and recorded;
- (d) prescribing methods to be adopted for securing adequate ventilation and cooling of the air in the workrooms.
- (2) In any factory in which the humidity of the air is artificially increased, the water used for the purpose shall be taken from a public supply, or other source of drinking water, or shall be effectively purified before it is so used.
- (3) If it appears to an Inspector that the water used in a factory for increasing humidity which is required to be effectively purified under sub-section (2) is not effectively purified he may serve on the manager of the factory an order in writing, specifying the measures which in his opinion should be adopted, and requiring them to be carried out before specified date.

VI. OVERCROWDING

- (1) No room in any factory shall be overcrowded to an extent injurious to the health of the workers employed therein.
- (2) Without prejudice to the generality of sub-section (1), there shall be in every workroom of a factory in existence on the date of the commencement of this Act at least 9.9 cubic metres and of a factory built after the commencement of this Act at least 14.2 cubic metres or space for every worker employed therein, and for the purposes of this sub-section no account shall be taken of any space which is more than 4.2 metres above the level of the floor of the room.
- (3) If the Chief Inspector by order in writing so requires, there shall be posted in each workroom of a factory a notice specifying the maximum number of workers who may, in compliance with the provisions of this section, be employed in the room.
- (4) The Chief Inspector may by order in writing exempt, subject to such conditions, if any, as he may think fit to impose, any workroom from the provisions of this section, if he is satisfied that compliance therewith in respect of the room is unnecessary in the interest of the health of the workers employed therein.

VII. LIGHTING

- (1) In every part of a factory where workers are working or passing there shall be provided and maintained sufficient and suitable lighting, natural or artificial, or both.
- (2) In every factory all glazed windows and skylights used for the lighting of the workroom shall be kept clean on both the inner and outer surfaces and, so far as compliance with the provisions of any rules made, under sub-section (3) of section 13 will allow, free from obstruction.
- (3) In every factory effective provision shall, so far as is practicable, be made for the prevention of —
 - (a) glare, either directly from a source of light or by reflection from a smooth or polished surface;
 - (b) the formation of shadows to such an extent as to cause eye-strain or the risk of accident to any worker.
- (4) The State Government may prescribe standards of sufficient and suitable lighting for factories or for any class or description of factories or for any manufacturing process.

VIII. DRINKING WATER

- (1) In every factory effective arrangements shall be made to provide and maintain at suitable points conveniently situated for all workers employed therein a sufficient supply of wholesome drinking water.
- (2) All such points shall be legibly marked “drinking water” in a language understood by a majority of the workers employed in the factory, and no such point shall be situated within six metres of any washing place, urinal, latrine, spittoon, open drain carrying sullage or effluent or any other source of contamination unless a shorter distance is approved in writing by the Chief Inspector.
- (3) In every factory wherein more than two hundred and fifty workers are ordinarily employed, provisions shall be made for cooling drinking water during hot weather by effective means and for distribution thereof.



- (4) In respect of all factories or any class or description of factories the State Government may make rules for securing compliance with the provisions of sub-sections (1), (2) and (3) and for the examination by prescribed Authorities of the supply and distribution of drinking water in factories.

IX. LATRINES AND URINALS

- (1) In every factory—
- (a) Sufficient latrine and urinal accommodation of prescribed types shall be provided conveniently situated and accessible to workers at all times while they are at the factory;
 - (b) Separate enclosed accommodation shall be provided for male and female workers;
 - (c) Such accommodation shall be adequately lighted and ventilated, and no latrine or urinal shall, unless specially exempted in writing by the Chief Inspector, communicate with any workroom except through an intervening open space or ventilated passage;
 - (d) All such accommodation shall be maintained in a clean and sanitary condition at all times;
 - (e) Sweepers shall be employed whose primary duty would be to keep clean latrines, urinals and washing places.
- (2) In every factory wherein more than two hundred and fifty workers are ordinarily employed—
- (a) All latrine and urinal accommodation shall be of prescribed sanitary types;
 - (b) The floors and internal walls, up to a height of ninety centimeters, of the latrines and urinals and the sanitary blocks shall be laid in glazed tiles or otherwise finished to provide a smooth polished impervious surface;
 - (c) Without prejudice to the provisions of clauses (d) and (e) of sub-section (1), the floors, portions of the walls and blocks so laid or finished and the sanitary pans of latrines and urinals shall be thoroughly washed and cleaned at least once in every seven days with suitable detergents or disinfectants or with both.
- (3) The State Government may prescribe the number of latrines and urinals to be provided in any factory in proportion to the numbers of male and female workers ordinarily employed therein, and provide for such further matters in respect of sanitation in factories, including the obligation of workers in this regard, as it considers necessary in the interest of the health of the workers employed therein.

X. SPITTOONS

- (1) In every factory there shall be provided a sufficient number of spittoons in convenient places and they shall be maintained in a clean and hygienic condition.
- (2) The State Government may make rules prescribing the type and the number of spittoons to be provided and their location in any factory and provide for such further matters relating to their maintenance in a clean and hygienic condition.
- (3) No person shall spit within the premises of a factory except in the spittoons provided for the purpose and a notice containing this provision and the penalty for its violation shall be prominently displayed at suitable places in the premises.
- (4) Whoever spits in contravention of sub-section (3) shall be punishable with fine not exceeding five rupees.

SAFETY

1. FENCING OF MACHINERY

- (1) In every factory the following, namely,—
- (i) Every moving part of a prime mover and every flywheel connected to a prime mover, whether the prime mover or flywheel is in the engine house or not;
 - (ii) The headrace and tailrace of every water-wheel and water turbine;
 - (iii) Any part of a stock-bar which projects beyond the head stock of a lathe; and
 - (iv) Unless they are in such position or of such construction as to be safe to every person employed in the factory as they would be if they were securely fenced, the following, namely—



- (a) every part of an electric generator, a motor or rotary converter;
- (b) every part of transmission machinery; and
- (c) every dangerous part of any other machinery, shall be securely fenced by safeguards of substantial construction which shall be constantly maintained and kept in position while the parts of machinery they are fencing are in motion or in use :

Provided that for the purpose of determining whether any part of machinery is in such position or is of such construction as to be safe as aforesaid, account shall not be taken of any occasion when—

- (i) it is necessary to make an examination of any part of the machinery aforesaid while it is in motion or, as a result of such examination, to carry out lubrication or other adjusting operation while the machinery is in motion, being an examination or operation which it is necessary to be carried out while that part of the machinery is in motion, or
 - (ii) in the case of any part of a transmission machinery used in such process as may be prescribed (being a process of a continuous nature the carrying on of which shall be, or is likely to be, substantially interfered with by the stoppage of that part of the machinery), it is necessary to make an examination of such part of the machinery while it is in motion or, as a result of such examination, to carry out any mounting or shipping of belts or lubrication or other adjusting operation while the machinery is in motion, and such examination or operation is made or carried out in accordance with the provisions of sub-section (1) of section 22.
- (2) The State Government may by rules prescribe such further precautions as it may consider necessary in respect of any particular machinery or part thereof, or exempt, subject to such condition as may be prescribed, for securing the safety of the workers, any particular machinery or part thereof from the provisions of this section.

2. WORK ON OR NEAR MACHINERY IN MOTION

- (1) Where in any factory it becomes necessary to examine any part of machinery referred to in section 21, while the machinery is in motion, or, as a result of such examination, to carry out –
- (a) In a case referred to in clause (i) of the proviso to sub-section (1) of section 21, lubrication or other adjusting operation; or
 - (b) In a case referred to in clause (ii) of the proviso aforesaid, any mounting or shipping of belts or lubrication or other adjusting operation, while the machinery is in motion such examination or operation shall be made or carried out only by a specially trained adult male worker wearing tight fitting clothing (which shall be supplied by the occupier) whose name has been recorded in the register prescribed in this behalf and who has been furnished with a certificate of his appointment, and while he is so engaged, -
 - (i) The belt is not more than fifteen centimeters in width;
 - (ii) The pulley is normally for the purpose of drive and not merely a fly-wheel or balance wheel (in which case a belt is not permissible);
 - (iii) The belt joint is either laced or flush with the belt;
 - (iv) The belt, including the joint and the pulley rim, are in good repair;
 - (v) There is reasonable clearance between the pulley and any fixed plant or structure;
 - (vi) Secure foothold and, where necessary, secure handhold, are provided for the operator; and
 - (vii) Any ladder in use for carrying out any examination or operation aforesaid is securely fixed or lashed or is firmly held by a second person.
 - (c) without prejudice to any other provision of this Act relating to the fencing of machinery, every set screw, bolt and key on any revolving shaft, spindle, wheel or pinion, and all spur, worm and other toothed or friction gearing in motion with which such worker would otherwise be liable to come into contact, shall be securely fenced to prevent such contact.
- (2) No woman or young person shall be allowed to clean, lubricate or adjust any part of a prime mover or of any transmission machinery while the prime mover or transmission machinery is in motion, or to clean,



lubricate or adjust any part of any machine if the cleaning, lubrication or adjustment thereof would expose the woman or young person to risk of injury from any moving part either of that machine or of any adjacent machinery.

- (3) The State Government may, by notification in the official. Gazette, prohibit, in any specified factory or class or description of factories, the cleaning, lubricating or adjusting by any person of specified parts of machinery when those parts are in motion.

3. EMPLOYMENT OF YOUNG PERSONS ON DANGEROUS MACHINES

- (1) No young person shall be required or allowed to work at any machine to which this section applies, unless he has been fully instructed as to the dangers arising in connection with the machine and the precautions to be observed and—
 - (a) has received sufficient training in work at the machine, or
 - (b) is under adequate supervision by a person who has a thorough knowledge and experience of the machine. (2) Sub-section (1) shall apply to such machines as may be prescribed by the State Government, being machines which in its opinion are of such a dangerous character that young persons ought not to work at them unless the foregoing requirements are complied with.

4. STRIKING GEAR AND DEVICES FOR CUTTING OFF POWER

- (1) In every factory—
 - (a) suitable striking gear or other efficient mechanical appliance shall be provided and maintained and used to move driving belts to and from fast and loose pulleys which form part of the transmission machinery, such gear or appliances shall be so constructed, placed and maintained as to prevent the belt from creeping back on to the fast pulley;
 - (b) driving belts when not in use shall not be allowed to rest or ride upon shafting in motion.
- (2) In every factory suitable devices for cutting off power in emergencies from running machinery shall be provided and maintained in every work-room:
Provided that in respect of factories in operation before the commencement of this Act, the provisions of this sub-section shall apply only to work-rooms in which electricity is used as power.
- (3) When a device, which can inadvertently shift from “off” to “on” position, is provided in a factory to cut off power, arrangements shall be provided for locking the device in safe position to prevent accidental starting of the transmission machinery or other machines to which the device is fitted.

5. SELF-ACTING MACHINES

No traversing part of a self-acting machine in any factory and no material carried thereon shall, if the space over which it runs is a space over which any person is liable to pass, whether in the course of his employment or otherwise, be allowed to run on its outward or inward traverse within a distance of forty-five centimeters from any fixed structure which is not part of the machine :

Provided that the Chief Inspector may permit the continued use of a machine installed before the commencement of this Act which does not comply with the requirements of this section on such conditions for ensuring safety as he may think fit to impose.

6. CASING OF NEW MACHINERY

- (1) In all machinery driven by power and installed in any factory after the commencement of this Act,—
 - (a) every set screw, bolt or key on any revolving shaft, spindle, wheel pinion shall be so sunk, encased or otherwise effectively guarded as to prevent danger;
 - (b) all spur, worm and other toothed or friction gearing which does not require frequent adjustment while in motion shall be completely encased, unless it is so situated as to be as safe as it would be if it were completely encased.



- (2) Whoever sells or lets on hire or, as agent of a seller or hirer, causes or procures to be sold on let or hire, for use in a factory any machinery driven by power which does not comply with the provisions of Sub-section (1) or any rules made under sub-section (3), shall be punishable with imprisonment for a term which may extend to three months or with fine which may extend to five hundred rupees or with both.
- (3) The State Government may make rules specifying further safeguards to be provided in respect of any other dangerous part of any particular machine or class or description of machines.

7. PROHIBITION OF EMPLOYMENT OF WOMEN AND CHILDREN NEAR COTTON-OPENERS

No woman or child shall be employed in any part of a factory for pressing cotton in which a cotton-opener is at work :

Provided that if the feed-end of a cotton-opener is in a room separated from the delivery end by a partition extending to the roof or to such height as the Inspector may in any particular case specify in writing, women and children may be employed on the side of the partition where the feed-end is situated.

8. HOISTS AND LIFTS

- (1) In every factory—
 - (a) every hoist and lift shall be—
 - (i) of good mechanical construction, sound material and adequate strength;
 - (ii) properly maintained, and shall be thoroughly examined by a competent person at least once in every period of six months, and a register shall be kept containing the prescribed particulars of every such examination;
 - (b) every hoistway and liftway shall be sufficiently protected by an enclosure fitted with gates, and the hoist or lift and every such enclosure shall be so constructed as to prevent any person or thing from being trapped between any part of the hoist or lift and any fixed structure or moving part;
 - (c) the maximum safe working load shall be plainly marked on every hoist or lift, and no load greater than such load shall be carried thereon;
 - (d) the cage of every hoist or lift used for carrying persons shall be fitted with a gate on each side from which access is afforded to a landing;
 - (e) every gate referred to in clause (b) or clause (a) shall be fitted with interlocking or other efficient device to secure that the gate cannot be opened except when the cage is at the landing and that the cage cannot be moved unless the gate is closed.
- (2) The following additional requirements shall apply to hoists and lifts used for carrying persons and installed or reconstructed in a factory after the commencement of this Act, namely :
 - (a) where the cage is supported by rope or chain, there shall be at least two ropes or chains separately connected with the cage and balance weight, and each rope or chain with its attachments shall be capable of carrying the whole weight of the cage together with its maximum load;
 - (b) efficient devices shall be provided and maintained capable of supporting the cage together with its maximum load in the event of breakage of the ropes, chains or attachments;
 - (c) an efficient automatic device shall be provided and maintained to prevent the cage from over-running.
- (3) The Chief Inspector may permit the continued use of a hoist or lift installed in a factory before the commencement of this Act which does not fully comply with the provisions of sub-section (1) upon such conditions for ensuring safety as he may think fit to impose.
- (4) The State Government may, if in respect of any class or description of hoist or lift, it is of opinion that it would be unreasonable to enforce any requirement of sub-sections. (1) and (2), by order direct that such requirement shall not apply to such class or description of hoist or lift.

Explanation : For the purposes of this section, no lifting machine or appliance shall be deemed to be a hoist or lift unless it has a platform or cage, the direction or movement of which is restricted by a guide or guides.



9. LIFTING MACHINES, CHAINS, ROPES AND LIFTING TACKLES

- (1) In any factory the following provisions shall be complied with in respect of every lifting machine (other than a hoist and lift) and every chain, rope and lifting tackle for the purpose of raising or lowering persons, goods or materials :-
 - (a) all parts, including the working gear, whether fixed or movable, of every lifting machine and every chain, rope or lifting tackle shall be—
 - (i) of good construction, sound material and adequate strength and free from defects;
 - (ii) properly maintained; and
 - (iii) thoroughly examined by a competent person at least once in every period of twelve months, or at such intervals as the Chief Inspector may specify in writing, and a register shall be kept containing the prescribed particulars of every such examination;
 - (b) no lifting machine and no chain, rope or lifting tackle shall, except for the purpose of test, be loaded beyond the safe working load which shall be plainly marked thereon together with an identification mark and duly entered in the prescribed register, and where this is not practicable, a table showing the safe working loads of every kind and size of lifting machine or, chain, rope or lifting tackle in use shall be displayed in prominent positions on the premises;
 - (c) while any person is employed or working on or near the wheel track of a travelling crane in any place where he would be liable to be struck by the crane, effective measures shall be taken to ensure that the crane does not approach within [1ra-66 six metres 1ra-66] of that place.
- (2) The State Government may make rules in respect of any lifting machine or any chain, rope or lifting tackle used in factories—
 - (a) prescribing further requirements to be complied with in addition to those set out in this section;
 - (b) providing for exemption from compliance with all or any of the requirements of this section, where in its opinion, such compliance is unnecessary or impracticable.
- (3) For the purposes of this section a lifting machine or a chain, rope or lifting tackle shall be deemed to have been thoroughly examined if a visual examination supplemented, if necessary, by other means and by the dismantling of parts of the gear, has been carried out as carefully as the conditions permit in order to arrive at a reliable conclusion as to the safety of the parts examined. Explanation : In this section,—
 - (a) “lifting machine” means a crane, crab, winch, teagle, pulley block, gin wheel, transporter or runway;
 - (b) “lifting tackle” means any chain, sling, rope sling, hook, shackle, swivel, coupling, socket, clamp, tray or similar appliance, whether fixed or movable, used in connection with the raising or lowering of persons, or loads by use of lifting machines.

10. REVOLVING MACHINERY

- (1) In every factory in which the process of grinding is carried on there shall be permanently affixed to or placed near each machine in use a notice indicating the maximum safe working peripheral speed of every grindstone or abrasive wheel, the speed of the shaft or spindle upon which the wheel is mounted, and the diameter of the pulley upon such shaft or spindle necessary to secure such safe working peripheral speed.
- (2) The speeds indicated in notices under sub-section (1) shall not be exceeded.
- (3) Effective measures shall be taken in every factory to ensure that the safe working peripheral speed of every revolving vessel, cage, basket, flywheel, pulley, disc or similar appliance driven by power is not exceeded.

11. PRESSURE PLANT

- (1) If in any factory, any plant or machinery or any part thereof is operated at a pressure above atmospheric pressure, effective measures shall be taken to ensure that the safe working pressure of such plant or machinery or part is not exceeded.
- (2) The State Government may make rules providing for the examination and testing of any plant or machinery



such as is referred to in sub-section (1) and prescribing such other safety measures in relation thereto as may in its opinion be necessary in any factory or class or description of factories.

- (3) The State Government may, by rules, exempt, subject to such conditions as may be specified therein, any part of any plant or machinery referred to in sub-section (1) from the provisions of this section.

12. FLOORS, STAIRS AND MEANS OF ACCESS

In every factory—

- (a) All floors, steps, stairs, passages and gangways shall be of sound construction and properly maintained and shall be kept free from obstructions and substances likely to cause persons to slip, and where it is necessary to ensure safety, steps, stairs, passages and gangways shall be provided with substantial handrails;
- (b) There shall, so far as is reasonably practicable, be provided and maintained safe means of access to every place at which any person is at any time required to work,
- (c) When any person has to work at a height from where he is likely to fall, provision shall be made, so far as is reasonably practicable, by fencing or otherwise, to ensure the safety of the person so working.

13. PITS, SUMPS, OPENINGS IN FLOORS, ETC

- (1) In every factory fixed vessel, sump, tank, pit or opening in the ground or in a floor which, by reasons of its depth, situation, construction or contents, is or may be a source of danger, shall be either securely covered or securely fenced.
- (2) The State Government may, by order in writing, exempt, subject to such conditions as may be prescribed, any factory or class or description of factories in respect of any vessel, sump, tank, pit or opening from compliance with the provisions of this section.

14. EXCESSIVE WEIGHTS

- (1) No person shall be employed in any factory to lift, carry or move any load so heavy as to be likely to cause him injury.
- (2) The State Government may make rules prescribing the maximum weights which may be lifted, carried or moved by adult men, adult women, adolescents and children employed in factories or in any class or description of factories or in carrying on any specified process.

15. PROTECTION OF EYES

In respect of any such manufacturing process carried on in any factory as may be prescribed, being a process which involves—

- (a) risk of injury to the eyes from particles or fragments thrown off in the course of the process, or
- (b) risk to the eyes by reason of exposure to excessive light, the State Government may by rules require that effective screens or suitable goggles shall be provided for the protection of persons employed on, or in the immediate vicinity of, the process.

16. PRECAUTIONS AGAINST DANGEROUS FUMES, GASES, ETC

- (1) No person shall be required or allowed to enter any chamber, tank, vat, pit, pipe, flue or other confined space in any factory in which any gas, fume, vapour or dust is likely to be present to such an extent as to involve risk to persons being overcome thereby, unless it is provided with a manhole of adequate size or other effective means of egress.
- (2) No person shall be required or allowed to enter any confined space as is referred to in sub-section (1), until all practicable measures have been taken to remove any gas, fume, vapour or dust, which may be present so as to bring its level within the permissible limits and to prevent any ingress of such gas, fume, vapour or dust and unless—



- (a) a certificate in writing has been given by a competent person, based on a test carried out by himself that the space is reasonably free from dangerous gas, fume, vapour or dust; or
- (b) such person is wearing suitable breathing apparatus and a belt securely attached to a rope the free end of which is held by a person outside the confined space.

17. PRECAUTIONS REGARDING THE USE OF PORTABLE ELECTRIC LIGHT

In any factory —

- (a) no portable electric light or any other electric appliance of voltage exceeding twenty-four volts shall be permitted for use inside any chamber, tank, vat, pit, pipe, flue or other confined space unless adequate safety devices are provided; and
- (b) if any inflammable gas, fume or dust is likely to be present in such chamber, tank, vat, pit, pipe, flue or other confined space, no lamp or light other than that of flame-proof construction shall be permitted to be used therein.

18. EXPLOSIVE OR INFLAMMABLE DUST, GAS, ETC

- (1) Where in any factory any manufacturing process produces dust, gas, fume or vapour of such character and to such extent as to be likely to explode to ignition, all practicable measures shall be taken to prevent any such explosion by—
 - (a) effective enclosure of the plant or machinery used in the process;
 - (b) removal or prevention of the accumulation of such dust, gas, fume or vapour;
 - (c) exclusion or effective enclosure of all possible sources of ignition.
- (2) Where in any factory the plant or machinery used in a process such as is referred to in sub-section (1) is not so constructed as to withstand the probable pressure which such an explosion as aforesaid would produce, all practicable measures shall be taken to restrict the spread and effects of the explosion by the provisions in the plant or machinery of chokes, baffles, vents or other effective appliances.
- (3) Where any part of the plant or machinery in a factory contains any explosive or inflammable gas or vapour under pressure greater than atmospheric pressure, that part shall not be opened except in accordance with the following provisions, namely :-
 - (a) before the fastening of any joint of any pipe connected with the part of the fastening of the cover of any opening into the part is loosened, any flow of the gas or vapour into the part of any such pipe shall be effectively stopped by a stop valve or other means;
 - (b) before any such fastening as aforesaid is removed, all practicable measures shall be taken to reduce the pressure of the gas or vapour in the part or pipe to atmospheric pressure;
 - (c) where any such fastening as aforesaid has been loosened or removed effective measures shall be taken to prevent any explosive or inflammable gas or vapour from entering the part of pipe until the fastening has been secured, or, as the case may be, securely replaced: Provided that the provisions of this sub-section shall not apply in the case of plant or machinery installed in the open air.
- (4) No plant, tank or vessel which contains or has contained any explosive or inflammable substance shall be subjected in any factory to any welding, brazing, soldering or cutting operation which involves the application of heat unless adequate measures have first been taken to remove such substance and any fumes arising therefrom or to render such substance and fumes non-explosive or non-inflammable, and no such substance shall be allowed to enter such plant, tank or vessel after any such operation until the metal has cooled sufficiently to prevent any risk of igniting the substance.
- (5) The State Government may by rules exempt, subject to such conditions as may be prescribed, any factory or class or description of factories from compliance with all or any of the provisions of this section.

19. PRECAUTIONS IN CASE OF FIRE

- (1) In every factory, all practicable measures shall be taken to prevent outbreak of fire and its spread, both internally and externally, and to provide and maintain - (a) safe means of escape for all persons in the event of a fire, and (b) the necessary equipment and facilities for extinguishing fire.



- (2) Effective measures shall be taken to ensure that in every factory all the workers are familiar with the means of escape in case of fire and have been adequately trained in the routine to be followed in such cases.
- (3) The State Government may make rules, in respect of any factory or class or description of factories, requiring the measures to be adopted to give effect to the provisions of sub-sections (1) and (2).
- (4) Notwithstanding anything contained in clause (a) of sub-section (1) or sub-section (2), if the Chief Inspector, having regard to the nature of the work carried on in any factory, the construction of such factory, special risk to life or safety, or any other circumstances, is of the opinion that the measures provided in the factory, whether as prescribed or not, for the purposes of clause (a) of sub-section (1) or sub-section (2), are inadequate, he may, by, order in writing, require that such additional measures as he may consider reasonable and necessary, be provided in the factory before such date as is specified in the order.

20. POWER TO REQUIRE SPECIFICATIONS OF DEFECTIVE PARTS OR TESTS OF STABILITY

If it appears to the Inspector that any building or part of a building or any part of the ways, machinery or plant in a factory is in such a condition that it may be dangerous to human life or safety, he may serve on the occupier or manager or both of the factory an order in writing requiring him before a specified date—

- (a) to furnish such drawings, specifications and other particulars as may be necessary to determine whether such building, ways, machinery or plant can be used with safety, or
- (b) to carry out such test in such manner as may be specified in the order, and to inform the Inspector of the results thereof.

21. SAFETY OF BUILDINGS AND MACHINERY

- (1) If it appears to the Inspector that any building or part of a building or any part of the ways, machinery or plant in a factory is in such a condition that it is dangerous to human life or safety, he may serve on the occupier or manager or both of the factory an order in writing specifying the measures which in his opinion should be adopted, and requiring them to be carried out before a specified date.
- (2) If it appears to the Inspector that the use of any building or part of a building or any part of the ways, machinery or plant in a factory involves imminent danger to human life or safety, he may serve on the occupier or manager or both of the factory an order in writing prohibiting its use until it has been properly repaired or altered.

22. MAINTENANCE OF BUILDINGS

If it appears to the Inspector that any building or part of a building in a factory is in such a state of disrepair as is likely to lead to conditions detrimental to the health and welfare of the workers, he may serve on the occupier or manager or both of the factory an order in writing specifying the measures which in his opinion should be taken and requiring the same to be carried out before such date as is specified in the order.

23. SAFETY OFFICERS

- (1) In every factory,—
 - (i) wherein one thousand or more workers are ordinarily employed, or
 - (ii) wherein, in the opinion of the State Government, any manufacturing process or operation is carried on, which process or operation involves any risk of bodily injury, poisoning or disease, or any other hazard to health, to the persons employed in the factory, the occupier shall, if so required by the State Government by notification in the Official Gazette, employ such number of Safety Officers as may be specified in that notification.
- (2) The duties, qualifications and conditions of service of Safety Officers shall be such as may be prescribed by the State Government.



Power to make rule to supplement the above listed provisions (Sec. 41)

The State Government may make rules requiring the provision in any factory or in any class or description of factories of such further devices and measures for securing the safety of persons employed therein as it may deem necessary.

PROVISIONS RELATING TO HAZARDOUS PROCESSES

(Sec. 41A to 41H, as introduced by Amendment Act 1987)

CONSTITUTION OF SITE APPRAISAL COMMITTEES (41-A)

- (1) The State Government may, for purposes of advising it to consider applications for grant of permission for the initial location of a factory involving a hazardous process or for the expansion of any such factory, appoint a Site Appraisal Committee consisting of—
 - (a) the Chief Inspector of the State who shall be its Chairman;
 - (b) a representative of the Central Board for the Prevention and Control of Water Pollution appointed by the Central Government under section 3 of the Water (Prevention and Control of Pollution) Act, 1974 (6 of 1974);
 - (c) a representative of the Central Board for the Prevention and Control of Air Pollution referred to in section 3 of the Air (Prevention and Control of Pollution) Act, 1981 (14 of 1981);
 - (d) a representative of the State Board appointed under section 4 of the Water (Prevention and Control of Pollution) Act, 1974 (6 of 1974);
 - (e) a representative of the State Board for the Prevention and Control of Air Pollution referred to in section 5 of the Air (Prevention and Control of Pollution) Act, 1981 (14 of 1981);
 - (f) a representative of the Department of Environment in the State;
 - (g) a representative of the Meteorological Department of the Government of India;
 - (h) an expert in the field of occupational health; and
 - (i) a representative of the Town Planning Department of the State Government, and not more than five other members who may be co-opted by the State Government who shall be—
 - (i) a scientist having specialised knowledge of the hazardous process which will be involved in the factory,
 - (ii) a representative of the local authority within whose jurisdiction the factory is to be established, and
 - (iii) not more than three other persons as deemed fit by the State Government.
- (2) The Site Appraisal Committee shall examine an application for the establishment of a factory involving hazardous process and make its recommendation to the State Government within a period of ninety days of the receipt of such applications in the prescribed form.
- (3) Where any process relates to a factory owned or controlled by the Central Government or to a corporation or a company owned or controlled by the Central Government, the State Government shall co-opt in the Site Appraisal Committee a representative nominated by the Central Government as a member of that Committee.
- (4) The Site Appraisal Committee shall have power to call for any information from the person making an application for the establishment or expansion of a factory involving a hazardous process.
- (5) Where the State Government has granted approval to an application for the establishment or expansion of a factory involving hazardous process, it shall not be necessary for an applicant to obtain a further approval from the Central Board or the State Board established under the Water (Prevention and Control of Pollution) Act 1974 (6 of 1974) and the Air (Prevention and Control of Pollution) Act, 1981 (14 of 1981).

COMPULSORY DISCLOSURE OF INFORMATION BY THE OCCUPIER (Sec 41-B)

- (1) The occupier of every factory involving a hazardous process shall disclose in the manner prescribed, all information regarding dangers, including health hazards and the measures to overcome such hazards



arising from the exposure to or handling of the materials or substances in the manufacture, transportation, storage and other processes, to the workers employed in the factory, the Chief Inspector, the local authority within whose jurisdiction the factory is situate and the general public in the vicinity.

- (2) The occupier shall, at the time of registering the factory involving a hazardous process, lay down a detailed policy with respect to the health and safety of the workers employed therein and intimate such policy to the Chief Inspector and the local Authority and, thereafter, at such intervals as may be prescribed, inform the Chief Inspector and the local Authority of any change made in the said policy.
- (3) The information furnished under sub-section (1) shall include accurate information as to the quantity, specifications and other characteristics of wastes and the manner of their disposal.
- (4) Every occupier shall, with the approval of the Chief Inspector, draw up an on-site emergency plan and detailed disaster control measures for his factory and make known to the workers employed therein and to the general public living in the vicinity of the factory the safety measures required to be taken in the event of an accident taking place.
- (5) Every occupier of a factory shall, - (a) if such factory engaged in a hazardous process on the commencement of the Factories (Amendment) Act, 1987 (2 of 1987), within a period of thirty days of such commencement; and (b) if such factory proposes to engage in a hazardous process at any time after such commencement, within a period of thirty days before the commencement of such process, inform the Chief Inspector of the nature and details of the process in such form and in such manner as may be prescribed.
- (6) Where any occupier of a factory contravenes the provisions of sub-section (5), the licence issued under section 6 to such factory shall, notwithstanding any penalty to which the occupier of factory shall be subjected to under the provisions of this Act, be liable for cancellation.
- (7) The occupier of a factory involving a hazardous process shall, with the previous approval of the Chief Inspector, lay down measures for the handling, usage, transportation and storage of hazardous substances inside the factory premises and the disposal of such substances outside the factory premises and publicise them in the manner prescribed among the workers and the general public living in the vicinity.

SPECIFIC RESPONSIBILITY OF THE OCCUPIER IN RELATION TO HAZARDOUS PROCESSES (Sec 41-C)

Every occupier of a factory involving any hazardous process shall—

- (a) Maintain accurate and up-to-date health records or, as the case may be, medical records, of the workers in the factory who are exposed to any chemical, toxic or any other harmful substances which are manufactured, stored, handled or transported and such records shall be accessible to the workers subject to such conditions as may be prescribed;
- (b) Appoint persons who possess qualifications and experience in handling hazardous substances and are competent to supervise such handling within the factory and to provide at the working place all the necessary facilities for protecting the workers in the manner prescribed: Provided that where any question arises as to the qualifications and experience of a person so appointed, the decision of the Chief Inspector shall be final;
- (c) Provide for medical examination of every worker -
 - (i) Before such worker is assigned to a job involving the handling of, or working with, a hazardous substance, and
 - (ii) While continuing in such job, and after he has ceased to work in such job, at intervals not exceeding twelve months, in such manner as may be prescribed.

POWER OF CENTRAL GOVERNMENT TO APPOINT INQUIRY COMMITTEE (Sec-41D)

- (1) The Central Government may, in the event of the occurrence of an extraordinary situation involving a factory engaged in a hazardous process, appoint an Inquiry Committee to inquire into the standards of health and safety observed in the factory with a view to finding out the causes of any failure or neglect in the adoption of any measures or standards prescribed for the health and safety of the workers employed in the factory or the general public affected, or likely to be affected, due to such failure or neglect and for the prevention and recurrence of such extraordinary situations in future in such factory or elsewhere.



- (2) The Committee appointed under sub-section (1) shall consist of a chairman and two other members and the terms of reference of the Committee and the tenure of office of its members shall be such as may be determined by the Central Government according to the requirements of the situation.
- (3) The recommendations of the Committee shall be advisory in nature.

EMERGENCY STANDARDS (Sec 41-E)

- (1) Where the Central Government is satisfied that no standards of safety have been prescribed in respect of a hazardous process or class of hazardous processes, or where the standards so prescribed are inadequate, it may direct the Director-General of Factory Advice Service and Labour Institutes or any institution specialised in matters relating to standards of safety in hazardous processes, to lay down emergency standards for enforcement of suitable standards in respect of such hazardous processes.
- (2) The emergency standards laid down under sub-section (1) shall, until they are incorporated in the rules made under this Act, be enforceable and have the same effect as if they had been incorporated in the rules made under this Act.

PERMISSIBLE LIMITS OF EXPOSURE OF CHEMICAL AND TOXIC SUBSTANCES (Sec 41-F)

- (1) The maximum permissible threshold limits of exposure of chemical and toxic substances in manufacturing processes (whether hazardous or otherwise) in any factory shall be of the value indicated in the Second Schedule.
- (2) The Central Government may, at any time, for the purpose of giving effect to any scientific proof obtained from specialised institutions or experts in the field,, by notification in the Official Gazette, make suitable changes in the said Schedule.

WORKERS' PARTICIPATION IN SAFETY MANAGEMENT (Sec 41-G)

- (1) The occupier shall, in every factory where a hazardous process takes place, or where hazardous substances are used or handled, set up a Safety Committee consisting of equal number of representatives of workers and management to promote cooperation between the workers and the management in maintaining proper safety and health at work and to review periodically the measures taken in that behalf : Provided that the State Government may, by order in writing and for reasons to be recorded, exempt the occupier of any factory or class of factories from setting up such committee.
- (2) The composition of the Safety Committee, the tenure of office of its members and their rights and duties shall be such as may be prescribed.

RIGHT OF WORKERS TO WARN ABOUT IMMINENT DANGER (Sec 41H)

- (1) Where the workers employed in any factory engaged in a hazardous process have reasonable apprehension that there is a likelihood of imminent danger to their lives or health due to any accident, they may bring the same to the notice of the occupier, agent, manager or any other person who is incharge of the factory or the process concerned directly or through their representatives in the Safety Committee and simultaneously bring the same to the notice of the Inspector.
- (2) It shall be the duty of such occupier, agent, manager or the person incharge of the factory or process to take immediate remedial action if he is satisfied about the existence of such imminent danger and send a report forthwith of the action taken to the nearest Inspector.
- (3) If the occupier, agent, manager or the person incharge referred to in sub-section (2) is not satisfied about the existence of any imminent danger as apprehended by the workers, he shall, nevertheless, refer the matter forthwith to the nearest Inspector whose decision on the question of the existence of such imminent danger shall be final.

**WELFARE (Sec 42-50)****WASHING FACILITIES (Sec 42)**

- (1) In every factory—
 - (a) adequate and suitable facilities for washing shall be provided and maintained for the use of the workers therein;
 - (b) separate and adequately screened facilities shall be provided for the use of male and female workers;
 - (c) such facilities shall be conveniently accessible and shall be kept clean.
- (2) The State Government may, in respect of any factory or class or description of factories or of any manufacturing process, prescribe standards of adequate and suitable facilities for washing.

FACILITIES FOR STORING AND DRYING CLOTHING (Sec 43)

The State Government may, in respect of any factory or class or description of factories, make rules requiring the provision therein of suitable places for keeping clothing not worn during working hours and for the drying of wet clothing.

FACILITIES FOR SITTING (Sec 44)

- (1) In every factory suitable arrangements for sitting shall be provided and maintained for all workers obliged to work in a standing position, in order that they may take advantage of any opportunities for rest which may occur in the course of their work.
- (2) If, in the opinion of the Chief Inspector, the workers in any factory engaged in a particular manufacturing process or working in a particular room are able to do their work efficiently in a sitting position, he may, by order in writing, require the occupier of the factory to provide before a specified date such seating arrangements as may be practicable for all workers so engaged or working.
- (3) The State Government may, by notification in the Official Gazette, declare that the provisions of subsection (1) shall not apply to any specified factory or class or description of factories or to any specified manufacturing process.

FIRST AID APPLIANCES (Sec 45)

- (1) There shall in every factory be provided and maintained so as to be readily accessible during all working hours first-aid boxes or cupboards equipped with the prescribed contents, and the number of such boxes or cupboards to be provided and maintained shall not be less than one for every one hundred and fifty workers ordinarily employed at any one time in the factory.
- (2) Nothing except the prescribed contents shall be kept in a first-aid box or cupboard.
- (3) Each first-aid box or cupboard shall be kept in the charge of a separate responsible person who holds a certificate in first-aid treatment recognized by State Government and who shall always be readily available during the working hours of the factory.
- (4) In every factory wherein more than five hundred workers are ordinarily employed there shall be provided and maintained an ambulance room of the prescribed size, containing the prescribed equipment and in the charge of such medical and nursing staff as may be prescribed and those facilities shall always be made readily available during the working hours of the factory.

CANTEENS (Sec 46)

- (1) The State Government may make rules requiring that in any specified factory wherein more than two hundred and, fifty workers are ordinarily employed, a canteen or canteens shall be provided and maintained by the occupier for the use of the workers.
- (2) Without prejudice to the generality of the foregoing power, such rules may provide for—
 - (a) The date by which such canteen shall be provided;
 - (b) The standards in respect of construction, accommodation, furniture and other equipment of the canteen;



- (c) The foodstuffs to be served therein and the charges which may be made therefor;
- (d) The constitution of a managing committee for the canteen and representation of the workers in the management of the canteen;
- (e) the items of expenditure in the running of the canteen which are not to be taken into account in fixing the cost of foodstuffs and which shall be borne by the employer;
- (f) the delegation to the Chief Inspector, subject to such conditions as may be prescribed, of the power to make rules under clause (c).

SHELTERS, REST ROOMS AND LUNCH ROOMS (Sec 47)

- (1) In every factory wherein more than one hundred and fifty workers are ordinarily employed, adequate and suitable shelters or rest rooms and a suitable lunch room, with provision for drinking water, where workers can eat meals brought by them, shall be provided and maintained for the use of the workers : Provided that any canteen maintained in accordance with the provisions of section 46 shall be regarded as part of the requirements of this sub-section : Provided further that where a lunch room exists no workers shall eat any food in the work room.
- (2) The shelters or rest rooms or lunch rooms to be provided under sub-section (1) shall be sufficiently lighted and ventilated and shall be maintained in a cool and clean condition.
- (3) The State Government may—
 - (a) prescribe the standards in respect of construction, accommodation, furniture and other equipment of shelters, rest rooms and lunch rooms to be provided under this section;
 - (b) by notification in the Official Gazette, exempt any factory or class or description of factories from the requirements of this section.

CRECHES (Sec 48)

- (1) In every factory wherein more than thirty women workers are ordinarily employed there shall be provided and maintained a suitable room or rooms for the use of children under the age of six years of such women.
- (2) Such rooms shall provide adequate accommodation, shall be adequately lighted and ventilated, shall be maintained in a clean and sanitary condition and shall be under the charge of women trained in the care of children and infants.
- (3) The State Government may make rules—
 - (a) prescribing the location and the standards in respect of construction, accommodation, furniture and other equipment of rooms to be provided, under this section;
 - (b) requiring the provision in factories to which this section applies of additional facilities for the care of children belonging to women workers, including suitable provision of facilities for washing and changing their clothing;
 - (c) requiring the provision in any factory of free milk or refreshment or both for such children;
 - (d) requiring that facilities shall be given in any factory for the mothers of such children to feed them at the necessary intervals.

WELFARE OFFICERS (Sec 49)

- (1) In every factory wherein five hundred or more workers are ordinarily employed the occupier shall employ in the factory such number of Welfare officers as may be prescribed.
- (2) The State Government may prescribe the duties, qualifications and Conditions of service of officers employed under sub-section (1).

POWER TO MAKE RULES (Sec 50)

The State Government may make rules—



- (a) Exempting, subject to compliance with such alternative arrangements for the welfare of workers as may be prescribed, any factory or class or description of factories from compliance with any of the provisions of this Chapter;
- (b) Requiring in any factory or class or description of factories that representatives of the workers employed in the factory shall be associated with the management of the welfare arrangements of the workers.

WORKING HOURS OF ADULTS

WEEKLY HOURS (Sec 51)

No adult workers shall be required or allowed to work in a factory for more than forty-eight hours in any week.

HOLIDAYS

WEEKLY HOLIDAYS (Sec 52)

- (1) No adult worker shall be required or allowed to work in a factory on the first day of the week (hereinafter referred to as the said day), unless—
 - (a) he has or will have a holiday for a whole day on one of the three days immediately before or after the said day, and
 - (b) the manager of the factory has, before the said day or the substituted day under clause.
 - (a) whichever is earlier,—
 - (i) delivered a notice at the office of the Inspector of his intention to require the worker to work on the said day and of the day which is to be substituted, and
 - (ii) displayed a notice to that effect in the factory : Provided that no substitution shall be made which will result in any worker working for more than ten days consecutively without a holiday for a whole day.
- (2) Notices given under sub-section (1) may be cancelled by a notice delivered at the office of the Inspector and a notice displayed in the factory not later than the day before the said day or the holiday to be cancelled, whichever is earlier.
- (3) Where, in accordance with the provisions of sub-section (1), any worker works on the said day and has had a holiday on one of the three days immediately before it, that said day shall, for the purpose of calculating his weekly hours of work, be included in the preceding week.

COMPENSATORY HOLIDAYS (Sec 53)

- (1) Where, as a result of the passing of an order or the making of a rule under the provisions of this Act exempting a factory or the workers therein from the provisions of section 52, a worker is deprived of any of the weekly holidays for which provision is made in sub-section (1) of that section, he shall be allowed, within the month in which the holidays were due to him or within the two months immediately following that month, compensatory holidays of equal number to the holidays so lost.
- (2) The State Government may prescribe the manner in which the holidays for which provision is made in sub-section (1) shall be allowed.

DAILY HOURS (Sec 54)

Subject to the provisions of section 51, no adult worker shall be required or allowed to work in a factory for more than nine hours in any day :

Provided that, subject to the previous approval of the Chief inspector, the daily maximum hours specified in this section may be exceeded in order to facilitate the change of shifts.

INTERVALS FOR REST (Sec 55)

- (1) The periods of work of adult workers in a factory each day shall be so fixed that no period shall exceed five hours and that no worker shall work for more than five hours before he has had an interval for rest of at least half an hour.



- (2) The State Government or, subject to the control of the State Government, the Chief Inspector, may, by written order and for the reasons specified therein, exempt any factory from the provisions of sub-section (1) so however that the total number of hours worked by a worker without an interval does not exceed six.

SPREADOVER (Sec 56)

The periods of work of an adult worker in a factory shall be so arranged that inclusive of his intervals for rest under section 55, they shall not spreadover more than ten and a half hours in any day : Provided that the Chief Inspector may, for reasons to be specified in in writing, increase the spreadover up to twelve hours.

NIGHT SHIFTS (Sec 57)

Where a worker in a factory works on a shift which extends beyond midnight,—

- (a) for the purposes of sections 52 and 53, a holiday for a whole day shall mean in his case a period of twenty-four consecutive hours beginning when his shift ends;
- (b) the following day for him shall be deemed to be the period of twenty-four hours beginning when such shift ends, and the hours he has worked after midnight shall be counted in the previous day.

PROHIBITION OF OVERLAPPING SHIFTS (Sec 58)

- (1) Work shall not be carried on in any factory by means of a system of shifts so arranged that more than one relay of workers is engaged, in work of the same kind at the same time.
- (2) The State Government or subject to the control of the State Government, the Chief Inspector, may, by written order and for the reasons specified therein, exempt on such conditions as may be deemed expedient, any factory or class or description of factories or any department or section of a factory or any category or description of workers therein from the provisions of sub-section (1).

EXTRA WAGES FOR OVERTIME (Sec 59)

- (1) Where a worker works in a factory for more than nine hours in any day or for more than forty-eight hours in any week, he shall, in respect of overtime work, be entitled to wages at the rate of twice his ordinary rate of wages.
- (2) For the purposes of sub-section (1), “ordinary rate of wages” means the basic wages plus such allowances, including the cash equivalent of the advantage accruing through the concessional sale to workers of foodgrains and other articles, as the worker is for the time being entitled to, but does not include a bonus and wages for overtime work.
- (3) Where any workers in a factory are paid on a piece-rate basis, the time rate shall be deemed to be equivalent to the daily average of their full-time earnings for the days on which they actually worked on the same or identical job during the month immediately preceding the calendar month during which the overtime work was done, and such time rates shall be deemed to be the ordinary rates of wages of those workers :

Provided that in the case of a worker who has not worked in the immediately preceding calendar month on the same or identical job, the time rate shall be deemed to be equivalent to the daily average of the earnings of the worker for the days on which he actually worked in the week in which the overtime work was done.

Explanation : For the purposes of this sub-section, in computing the earnings for the days on which the worker actually worked such allowances, including the cash equivalent of the advantage accruing through the concessional sale to workers of foodgrains and other articles, as the worker is for the time being entitled to, shall be included but any bonus or wages for overtime work payable in relation to the period with reference to which the earnings are being computed shall be excluded.

- (4) The cash equivalent of the advantage accruing through the concessional sale to a worker of foodgrains and other articles shall be computed as often as may be prescribed on the basis of the maximum quantity of foodgrains and other articles admissible to a standard family.

Explanation 1 : Standard family means a family consisting of the worker, his or her spouse and two children below the age of fourteen years requiring in all three adult consumption units.



Explanation 2 : Adult consumption unit means the consumption unit of a male above the age of fourteen years; and the consumption unit of a female above the age of fourteen years and that of a child below the age of fourteen years shall be calculated at the rates of 0.8 and 0.6 respectively of one adult consumption unit.

- (5) The State Government may make rules prescribing -
- (a) The manner in which the cash equivalent of the advantage accruing through the concessional sale to a worker of foodgrains and other articles shall be computed; and
 - (b) The registers that shall be maintained in a factory for the purpose of securing compliance with the provisions of this section.

RESTRICTION ON DOUBLE EMPLOYMENT (Sec 60)

No adult worker shall be required or allowed to work in any factory on any day on which he has already been working in any other factory, save in such circumstances as may be prescribed.

NOTICE OF PERIODS OF WORK FOR ADULTS (Sec 61)

- (1) There shall be displayed and correctly maintained in every factory in accordance with the provisions of sub-section (2) of section 108, a notice of periods of work for adults, showing clearly for every day the periods during which adult workers may be required to work.
- (2) The periods shown in the notice required by sub-section (1) shall be fixed beforehand in accordance with the following provisions of this section, and shall be such that workers working for those periods would not be working in contravention of any of the provisions of sections 51, 52, 53, 54, 55, 56 and 58.
- (3) Where all the adult workers in a factory are required to work during the same periods, the manager of the factory shall fix those periods for such workers generally.
- (4) Where all the adult workers in a factory are not required to work during the same periods, the manager of the factory shall classify them into groups according to the nature of their work indicating the number of workers in each group.
- (5) For each group which is not required to work on a system of shifts, the manager of the factory shall fix the periods during which the group may be required to work.
- (6) Where any group is required to work on a system of shifts and the relays are not to be subject to predetermined periodical changes of shifts, the manager of the factory shall fix the periods during which each relay of the group may be required to work.
- (7) Where any group is to work on a system of shifts and the relays are to be subject to predetermined periodical changes of shifts, the manager of the factory shall draw up a scheme of shifts whereunder the periods during which any relay of the group may be required to work and the relay which will be working at any time of the day shall be known for any day.
- (8) The State Government may prescribe forms of the notice required by sub-section (1) and the manner in which it shall be maintained.
- (9) In the case of a factory beginning work after the commencement of this Act, a copy of the notice referred to in sub-section (1) shall be sent in duplicate to the Inspector before the day on which work is begun in the factory.
- (10) Any proposed change in the system of work in any factory which will necessitate a change in the notice referred to in sub-section (1) shall be notified to the Inspector in duplicate before the change is made, and except with the previous sanction of the Inspector, no such change shall be made until one week has elapsed since the last change.

REGISTER OF ADULT WORKERS (Sec 62 and 63)

- (1) The manager of every factory shall maintain a register of adult workers, to be available to the Inspector at all times during working hours, or when any work is being carried on in the factory, showing—
 - (a) the name of each adult worker in the factory;
 - (b) the nature of his work;
 - (c) the group, if any, in which he is included;



- (d) where his group works on shifts, the relay to which he is allotted; and
- (e) such other particulars as may be prescribed :

Provided that if the Inspector is of opinion that any muster roll or register maintained as a part of the routine of a factory gives in respect of any or all the workers in the factory the particulars required under this section, he may, by order in writing, direct that such muster roll or register shall to the corresponding extent be maintained in place of, and be treated as, the register of adult workers in that factory.

- (1A) No adult worker shall be required or allowed to work in any factory unless his name and other particulars have been entered in the register of adult workers.
- (2) The State Government may prescribe the form of the register of adult workers, the manner in which it shall be maintained and the period for which it shall be preserved.

HOURS OF WORK TO CORRESPOND WITH NOTICE UNDER SECTION 61 AND REGISTER UNDER SECTION 62

No adult worker shall be required or allowed to work in any factory otherwise than in accordance with the notice of periods of work for adults displayed in the factory and the entries made beforehand against his name in the register of adult workers of the factory.

POWER TO MAKE EXEMPTING RULES

- (1) The State Government may make rules defining the persons who hold positions of supervisions or management or are employed in a confidential position in a factory or empowering the Chief inspector to declare any person, other than a person defined by such rules, as a person holding position of supervision or management or employed in a confidential position in a factory if, in the opinion of the Chief Inspector, such person holds such position or is so employed and the provisions of this chapter, other than the provisions of clause (b) of sub-section (1) of section 66 and of the proviso to that sub-section, shall not apply to any person so defined or declared :

Provided that any person so defined or declared shall, where the ordinary rate of wages of such person does not exceed the wage limit specified in sub-section (6) of section 1 of the Payment of Wages Act, 1936 (4 of 1936), as amended from time to time, be entitled to extra wages in respect of over time work under section 59.

- (2) The State Government may make rules in respect of adult workers in factories providing for the exemption, to such extent and subject to such conditions as may be prescribed.—
 - (a) of workers engaged on urgent repairs, from the provisions of sections 51, 52, 54, 55 and 56;
 - (b) of workers engaged in work in the nature of preparatory or complementary work which must necessarily be carried on outside the limits laid down for the general working of the factory, from the provisions of sections 51, 54, 55 and 56;
 - (c) of workers engaged in work which is necessarily so intermittent that the intervals during which they do not work while on duty ordinarily amount to more than the intervals for rest required by or under section 55, from the provisions of sections 51, 54, 55 and 56;
 - (d) of workers engaged, in ally work which for technical reasons must be carried on continuously from the provisions of sections 51, 52, 54, 55 and 56;
 - (e) of workers engaged in making or supplying articles of prime necessity which must be made or supplied every day, from the provisions of section 51, section 52;
 - (f) of workers engaged in a manufacturing process which cannot be carried on except during fixed seasons, from the provisions of section 51, section 52 and section 54;
 - (g) of workers engaged in a manufacturing process which cannot be carried on except at times dependent on the irregular action of natural forces, from the provisions of sections 52 and 55;
 - (h) of workers engaged in engine-rooms or boiler-houses or in attending to power-plant or transmission machinery, from the provisions of section 51 and section 52;
 - (i) of workers engaged in the printing of newspapers, who are held up on account of the breakdown of machinery, from the provisions of sections 51, 54 and 56.



Explanation : In this clause the expression newspapers has the meaning assigned to it in the Press and Registration of Books Act, 1867 (25 of 1867);

- (j) of workers engaged in the loading or unloading of railway wagons, or lorries or trucks [ra-106] from the provisions of sections 51, 52, 54, 55 and 56;
 - (k) of workers engaged in any work, which is notified by the State Government in the Official Gazette as a work of national importance, from the provisions of section 51, section 52, section 54, section 55 and section 56.
- (3) Rules made under sub-section (2) providing for any exemption may also provide for any consequential exemption from the provisions of section 61 which the State Government may deem to be expedient, subject to such conditions as it may prescribe.
- (4) In making rules under this section, the State Government shall not exceed, except in respect of exemption under clause (a) of sub-section (2), the following limits of work inclusive of overtime :-
- (i) the total number of hours of work in any day shall not exceed ten;
 - (ii) the spreadover, inclusive of intervals for rest, shall not exceed twelve hours in any one day;
- Provided that the State Government may, in respect of any or all of the categories of workers referred to in clause (d) of sub-section (2), make rules prescribing the circumstances in which, and the conditions subject to which, the restrictions imposed by clause (i) and clause (ii) shall not apply in order to enable a shift worker to work the whole or part of a subsequent shift in the absence of a worker who has failed to report for duty;
- (iii) the total number of hours of work in a week, including overtime shall not exceed sixty;
 - (iv) the total number of hours of overtime shall not exceed fifty for any one quarter. Explanation : "Quarter" means a period of three consecutive months beginning on the 1st of January, the 1st of April, the 1st of July or the 1st of October.
- (5) Rules made under this section shall remain in force for not more than five years.

POWER TO MAKE EXEMPTING ORDERS

- (1) Where the State Government is satisfied that, owing to the nature of the work carried on or to other circumstances, it is unreasonable to require that the periods of work of any adult workers in any factory or class or description of factories should be fixed beforehand, it may, by written order, relax or modify the provisions of section 61 in respect of such workers therein, to such extent and in such manner as it may think fit, and subject to such conditions as it may deem expedient to ensure control over periods of work.
- (2) The State Government or, subject to the control of the State Government, the Chief Inspector, may by written order exempt, on such conditions as it or he may deem expedient, any or all of the adult workers in any factory or group or class or description of factories from any or all of the provisions of sections, 51, 52, 54 and 56 on the ground that the exemption is required to enable the factory or factories to deal with an exceptional press of work.
- (3) Any exemption granted under sub-section (2) shall be subject to the following conditions, namely :-
- (i) The total number of hours of work in any day shall not exceed twelve;
 - (ii) The spread over, inclusive of intervals for rest, shall not exceed thirteen hours in any one day;
 - (iii) The total number of hours of work in any week, including overtime, shall not exceed sixty;
 - (iv) No worker shall be allowed to work overtime, for more than seven days at a stretch and the total number of hours of overtime work in any quarter shall not exceed seventy-five. Explanation: In this sub-section "quarter" has the same meaning as in sub-section
- (4) Of section 64.

FURTHER RESTRICTIONS ON EMPLOYMENT OF WOMEN

- (1) The provisions of this Chapter shall, in their application to women in factories, be supplemented by the following further restrictions, namely —
- (a) No exemption from the provisions of section 54 may be granted in respect of any women;
 - (b) No women shall be required or allowed to work in any factory except between the hours of 6 A.M. and 7 P.M. :



Provided that the State Government may, by notification in the Official Gazette, in respect of any factory or group or class or description of factories, vary the limits laid down in clause (b), but so that no such variation shall authorize the employment of any woman between the hours of 10 P.M. and 5 A.M.; [Ira-114 (c) there shall be no change of shifts except, after a weekly holiday or any other holiday.

- (2) The State Government may make rules providing for the exemption from the restrictions set out in sub-section (1), to such extent and subject to such conditions as it may prescribe, of women working in fish curing or fish-canning factories, where the employment of women beyond the hours specified in the said restrictions is necessary to prevent damage to or deterioration in, any raw material.
- (3) The rules made under sub-section (2) shall remain in force for not more than three years at a time.

PROHIBITION OF EMPLOYMENT OF YOUNG CHILDREN (Sec 67)

No child who has not completed his fourteenth year shall be required or allowed to work in any factory.

NON-ADULT WORKERS TO CARRY TOKENS (Sec 68)

A child who has completed his fourteenth year or an adolescent shall not be required or allowed to work in any factory unless—

- (a) a certificate of fitness granted with reference to him under section 69 is in the custody of the manager of the factory; and
- (b) such child or adolescent carries while he is at work a token giving a reference to such certificate.

CERTIFICATES OF FITNESS (Sec 69)

- (1) A certifying surgeon shall, on the application of any young person or his parent or guardian accompanied by a document signed by the manager of a factory that such person will be employed therein if certified to be fit for work in a factory, or on the application of the manager of the factory in which any young person wishes to work, examine such person and ascertain his fitness for work in a factory.
- (2) The certifying surgeon, after examination, may grant to such young person, in the prescribed form, or may renew –
 - (a) a certificate of fitness to work in a factory as a child, if he is satisfied that the young person has completed his fourteenth year, that he has attained the prescribed physical standards and that he is fit for such work;
 - (b) a certificate of fitness to work in a factory as an adult, if he is satisfied that the young person has completed his fifteenth year, and is fit for a full day's work in a factory :

Provided that unless the certifying surgeon has personal knowledge of the place where the young person proposes to work and of the manufacturing process in which he will be employed, he shall not grant or renew a certificate under this sub-section until he has examined such place.
- (3) A certificate of fitness granted or renewed under sub-section (2) -
 - (a) shall be valid only for a period of twelve months from the date thereof;
 - (b) may be made subject to conditions in regard to the nature of the work in which the young person may be employed, or requiring re-examination of the young person before the expiry of the period of twelve months.
- (4) A certifying surgeon shall revoke any certificate granted or renewed under sub-section (2) if in his opinion the holder of it is no longer fit to work in the capacity stated therein in a factory.
- (5) Where a certifying surgeon refuses to grant or renew a certificate or a certificate of the kind requested or revokes a certificate, he shall, if so requested by any person who could have applied for the certificate or the renewal thereof, state his reasons in writing for so doing.
- (6) Where a certificate under this section with reference to any young person is granted or renewed subject to such conditions as are referred to in clause (b) of sub-section (3), the young person shall not be required or allowed to work in any factory except in accordance with those conditions.
- (7) Any fee payable for a certificate under this section shall be paid by the occupier and shall not be recoverable from the young person, his parents or guardian.

**EFFECT OF CERTIFICATE OF FITNESS GRANTED TO ADOLESCENT**

- (1) An adolescent who has been granted a certificate of fitness to work in a factory as an adult under clause (b) of sub-section (2) of section 69, and who while at work in a factory carries a token giving reference to the certificate, shall be deemed to be an adult for all the purposes of Chapters VI and VII.
(1A) No female adolescent or a male adolescent who has not attained the age of seventeen years but who has been granted a certificate of fitness to work in a factory as an adult, shall be required or allowed to work in any factory except between 6 A.M. and 7 P.M. :
Provided that the State Government may, by notification in the Official Gazette, in respect of any factory or group or class or description of factories -
 - (i) vary the limits laid down in this sub-section so, however, that no such section shall authorise the employment of any female adolescent between 10 P.M. and 5 A.M.;
 - (ii) grant exemption from the provisions of this sub-section in case of serious emergency where national interest is involved.
- (2) An adolescent who has not been granted a certificate of fitness to work in a factory as an adult under the aforesaid clause (b) shall, notwithstanding his age, be deemed to be a child for all the purposes of this Act.

WORKING HOURS FOR CHILDREN

- (1) No child shall be employed or permitted to work, in any factory -
 - (a) for more than four and a half hours in any day;
 - (b) during the night. Explanation : For the purposes of this sub-section “night” shall mean a period of at least twelve consecutive hours which shall include the interval between 10 P.M. and 6 A.M.
- (2) The period of work of all children employed in a factory shall be limited to two shifts which shall not overlap or spread over more than five hours each; and each child shall be employed in only one of the relays which shall not, except with the previous permission in writing of the Chief Inspector, be changed more frequently than once in a period of thirty days.
- (3) The provisions of section 52 shall apply also to child workers and no exemption from the provisions of that section may be granted in respect of any child.
- (4) No child shall be required or allowed to work in any factory on any day on which he has already been working in another factory.
- (5) No female child shall be required or allowed to work in any factory except between 8 A.M. and 7 P.M.

NOTICE OF PERIODS OF WORK FOR CHILDREN

- (1) There shall be displayed and correctly maintained in every factory in which children are employed, in accordance with the provisions of sub-section (2) of section 108 a notice of period of work for children, showing clearly for every day the periods during which children may be required or allowed to work.
- (2) The periods shown in the notice required by sub-section (1) shall be fixed beforehand in accordance with the method laid down for adult workers in section 61, and shall be such that children working for those periods would not be working in contravention of any of the provisions of section 71.
- (3) The provisions of sub-sections (8), (9) and (10) of section 61 shall apply also to the notice required by sub-section (1) of this section.

REGISTER OF CHILD WORKERS

- (1) The manager of every factory in which children are employed shall maintain a register of child workers, to be available to the Inspector at all times during working hours or when any work is being carried on in a factory, showing—
 - (a) the name of each child worker in the factory,
 - (b) the nature of his work,
 - (c) the group, if any, in which he is included,
 - (d) where his group works in shifts, the relay to which he is allotted, and
 - (e) the number of his certificate of fitness granted under section 69.



- (1A) No child worker shall be required or allowed to work in any factory unless his name and other particulars have been entered in the register of child workers.
- (2) The State Government may prescribe the form of the register of child workers, the manner in which it shall be maintained and the period for which it shall be preserved.

HOURS OF WORK TO CORRESPOND WITH NOTICE UNDER SECTION 72 AND REGISTER UNDER SECTION 73

No child shall be employed in any factory otherwise than in accordance with the notice of periods of work for children displayed in the factory and the entries made beforehand against his name in the register of child workers of the factory.

POWER TO REQUIRE MEDICAL EXAMINATION

Where an Inspector is of opinion—

- (a) that any person working in a factory without a certificate of fitness is a young person, or
- (b) that a young person working in a factory with a certificate of fitness is no longer fit to work in the capacity stated therein, - he may serve on the manager of the factory a notice requiring that such person or young person, as the case may be, shall be examined by a certifying surgeon, and such person or young person shall not, if the Inspector so directs, be employed, or permitted to work, in any factory until he has been so examined and has been granted a certificate of fitness or a fresh certificate of fitness, as the case may be, under section 69, or has been certified by the certifying surgeon examining him not to be a young person.

POWER TO MAKE RULES

The State Government may make rules—

- (a) prescribing the forms of certificates of fitness to be granted under section 69, providing for the grant of duplicates in the event of loss of the original certificates, and fixing the fees which may be charged for such certificates and renewals thereof and such duplicates;
- (b) prescribing the physical standards to be attained by children and adolescents working in factories;
- (c) regulating the procedure of certifying surgeons under this Chapter;
- (d) specifying other duties which certifying surgeons may be required to perform in connection with the employment of young persons in factories, and fixing the fees which may be charged for such duties and the persons by whom they shall be payable.

CERTAIN OTHER PROVISIONS OF LAW NOT BARRED

The provisions of this Chapter shall be in addition to, and not in derogation of, the provisions of the Employment of Children Act, 1938 (26 of 1938).

APPLICATION OF CHAPTER

- (1) The provisions of this Chapter shall not operate to the prejudice of any right to which a worker may be entitled under any other law or under the terms of any award, agreement (including settlement) or contract of service :

Provided that if such award, agreement (including settlement) or contract of service provides for a longer annual leave with wages than provided in this Chapter, the quantum of leave, which the worker shall be entitled to, shall be in accordance with such award, agreement or contract of service but in relation to matters not provided for in such award, agreement or contract of service or matters which are provided for less favourably therein, the provisions of sections 79 to 82, so far as may be, shall apply.

- (2) The provisions of this Chapter shall not apply to workers in any factory of any railway administered by the Government, who are governed by leave rules approved by the Central Government.

ANNUAL LEAVE WITH WAGES

- (1) Every worker who has worked for a period of 240 days or more in a factory during a calendar year shall be allowed during the subsequent calendar year, leave with wages for a number of days calculated at the rate of -



- (i) if an adult, one day for every twenty days of work performed by him during the previous calendar year;
- (ii) if a child, one day for every fifteen days of work formed by him during the previous calendar year.

Explanation 1 : For the purpose of this sub-section—

- (a) any days of lay off, by agreement or contract or as permissible under the standing orders;
- (b) in the case of a female worker, maternity leave for any number of days not exceeding twelve weeks; and
- (c) the leave earned in the year prior to that in which the leave is enjoyed; shall be deemed to be days on which the worker has worked in a factory for the purpose of computation of the period of 240 days or more, but he shall not earn leave for these days.

Explanation 2 : The leave admissible under this sub-section shall be exclusive of all holidays whether occurring during or at either end of the period of leave.

- (2) A worker whose service commences otherwise than on the first day of January shall be entitled to leave with wages at the rate laid down in clause (i) or, as the case may be, clause (ii) of sub-section (1) if he has worked for two-thirds of the total number of days in the remainder of the calendar year.
- (3) If a worker is discharged or dismissed from service or quits his employment or is superannuated or dies while in service, during the course of the calendar year, he or his heir or nominee, as the case may be, shall be entitled to wages in lieu of the quantum of leave to which he was entitled immediately before his discharge, dismissal, quitting of employment, superannuation or death calculated at the rates specified in sub-section (1), even if he had not worked for the entire period specified in sub-section (1) or sub-section (2) making him eligible to avail of such leave, and such payment shall be made -
 - (i) where the worker is discharged or dismissed or quits employment, before the expiry of the second working day from the date of such discharge, dismissal or quitting, and
 - (ii) where the worker is superannuated or dies while in service, before the expiry of two months from the date of such superannuation or death.
- (4) In calculating leave under this section, fraction of leave of half a day or more shall be treated as one full day's leave, and fraction of less than half a day shall be omitted.
- (5) If a worker does not in any one calendar year take the whole of the leave allowed to him under sub-section (1) or sub-section (2), as the case may be, any leave not taken by him shall be added to the leave to be allowed to him in the succeeding calendar year :

Provided that the total number of days of leave that may be carried forward to a succeeding year shall not exceed thirty in the case of an adult or forty in the case of a child :

Provided further that a worker, who has applied for leave with wages but has not been given such leave in accordance with any scheme laid down in sub-sections (8) and (9) or in contravention of sub-section (10) shall be entitled to carry forward the leave refused without any limit.

- (6) A worker may at any time apply in writing to the manager of a factory not less than fifteen days before the date on which he wishes his leave to begin, to take all the leave or any portion thereof allowable to him during the calendar year :

Provided that the application shall be made not less than thirty days before the date on which the worker wishes his leave to begin, if he is employed in a public utility service as defined in clause (n) of section 2 of the Industrial Disputes Act, 1947 (14 of 1947) :

Provided further that the number of times in which leave may be taken during any year shall not exceed three.

- (7) If a worker wants to avail himself of the leave with wages due to him to cover a period of illness, he shall be granted such leave even if the application for leave is not made within the time specified in sub-section (6); and in such a case wages as admissible under section 81 shall be paid not later than fifteen days, or in the case of a public utility service not later than thirty days from the date of the application for leave.
- (8) For the purpose of ensuring the continuity of work, the occupier or manager of the factory, in agreement with the Works Committee of the factory constituted under section 3 of the Industrial Disputes Act, 1947



(14 of 1947), or a similar Committee constituted under any other Act or if there is no such Works Committee or a similar Committee in the factory, in agreement with the representatives of the workers therein chosen in the prescribed manner, may lodge with the Chief Inspector a scheme in writing whereby the grant of leave allowable under this section may be regulated.

- (9) A scheme lodged under sub-section (8) shall be displayed at some conspicuous and convenient places in the factory and shall be in force for a period of twelve months from the date on which it comes into force, and may thereafter be renewed with or without modification for a further period of twelve months at a time, by the manager in agreement with the Works Committee or a similar Committee, or as the case may be, in agreement with the representatives of the workers as specified in sub-section (8), and a notice of renewal shall be sent to the Chief Inspector before it is renewed.
- (10) An application for leave which does not contravene the provisions of sub-section (6) shall not be refused, unless refusal is in accordance with the scheme for the time being in operation under sub-sections (8) and (9).
- (11) If the employment of a worker who is entitled to leave under sub-section (1) or sub-section (2), as the case may be, is terminated by the occupier before he has taken the entire leave to which he is entitled, or if having applied for and having not been granted such leave, the worker quits his employment before he has taken the leave, the occupier of the factory shall pay him the amount payable under section 80 in respect of the leave not taken, and such payment shall be made, where the employment of the worker is terminated by the occupier, before the expiry of the second working day after such termination, and where a worker who quits his employment, on or before the next pay day.
- (12) The unavailed leave of a worker shall not be taken into consideration in computing the period of any notice required to be given before discharge or dismissal.

WAGES DURING LEAVE PERIOD

- (1) For the leave allowed to him under section 78 or section 79, as the case may be a worker shall be entitled to wages at a rate equal to the daily average of his total full time earnings for the days on which he actually worked during the month immediately preceding his leave, exclusive of any overtime and bonus but inclusive of dearness allowance and the cash equivalent of the advantage accruing through the concessional sale to the worker of foodgrains and other articles :

Provided that in the case of a worker who has not worked on any day during the calendar month immediately preceding his leave, he shall be paid at a rate equal to the daily average of his total full time earnings for the days on which he actually worked during the last calendar month preceding his leave, in which he actually worked, exclusive of any overtime and bonus but inclusive of dearness allowance and the cash equivalent of the advantage accruing through the concessional sale to the workers of foodgrains and other articles.

- (2) The cash equivalent of the advantage accruing through the concessional sale to the worker of foodgrains and other articles shall be computed as often as may be prescribed, on the basis of the maximum quantity of foodgrains and other articles admissible to a standard family.

Explanation 1 : “Standard family” means a family consisting of a worker, his or her spouse and two children below the age of fourteen years requiring in all three adult consumption units.

Explanation 2 : Adult consumption unit means the consumption unit of a male above the age of fourteen years; and the consumption unit of a female above the age of fourteen years and that of a child below the age of fourteen years shall be calculated at the rates of 0.8 and 0.6 respectively of one adult consumption unit.

- (3) The State Government may make rules prescribing—
 - (a) the manner in which the cash equivalent of the advantage accruing through the concessional sale to a worker of foodgrains and other articles shall be computed; and
 - (b) the registers that shall be maintained in a factory for the purpose of securing compliance with the provisions of this section.

PAYMENT IN ADVANCE IN CERTAIN CASES

A worker who has been allowed leave for not less than four days, in the case of an adult, and five days, in the case of a child, shall, before his leave begins, be paid the wages due for the period of the leave allowed.

**MODE OF RECOVERY OF UNPAID WAGES**

Any sum required to be paid by an employer, under this chapter but not paid by him shall be recoverable as delayed wages under the provisions of the Payment of Wages Act, 1936 (4 of 1936).

POWER TO MAKE RULES

The State Government may make rules directing managers of factories to keep registers containing such particulars as may be prescribed and requiring the registers to be made available for examination by Inspectors.

POWERS TO EXEMPT FACTORIES

Where the State Government is satisfied that the leave rules applicable to workers in a factory provide benefits which in its opinion are not less favourable than those for which this Chapter makes provision it may, by written order, exempt the factory from all or any of the provisions of this Chapter subject to such conditions as may be specified in the order.

Explanation : For the purposes of this section, in deciding whether the benefits which are provided for by any leave rules are less favourable than those for which this Chapter makes provision, or not, the totality of the benefits shall be taken into account.

POWER TO APPLY THE ACT TO CERTAIN PREMISES

- (1) The State Government may, by notification in the Official Gazette, declare that all or any of the provisions of this Act shall apply to any place wherein a manufacturing process is carried on with or without the aid of power or is so ordinarily carried on, notwithstanding that—
 - (i) the number of persons employed therein is less than ten, if working with the aid of power and less than twenty if working without the aid of power, or
 - (ii) the persons working therein are not employed by the owner thereof but are working with the permission of, or under agreement with, such owner : Provided that the manufacturing process is not being carried on by the owner only with the aid of his family.
- (2) After a place is so declared, it shall be deemed to be a factory for the purposes of this Act, and the owner shall be deemed to be the occupier, and any person working therein, a worker. Explanation : For the purposes of this section, owner shall include a lessee or mortgagee with possession of the premises.

POWER TO EXEMPT PUBLIC INSTITUTIONS

The State Government may exempt, subject to such conditions as it may consider necessary, any workshop or workplace where a manufacturing process is carried on and which is attached to a public institution, maintained for the purposes of education, training, research or reformation, from all or any of the provisions of this Act : Provided that no exemption shall be granted from the provisions relating to hours of work and holidays, unless the persons having the control of the institution submit, for the approval of the State Government, a scheme for the regulation of the hours of employment, intervals for meals, and holidays of the persons employed in or attending the institution or who are inmates of the institution, and the State Government is satisfied that the provisions of the scheme are not less favourable than the corresponding provisions of this Act.

DANGEROUS OPERATIONS

Where the State Government is of opinion that any manufacturing process or operation carried on in a factory exposes any persons employed in it to a serious risk of bodily injury, poisoning or diseases, it may make rules applicable to any factory or class or description of factories in, which the manufacturing process or operation is carried on—

- (a) Specifying the manufacturing process or operation and declaring it to be dangerous;
- (b) Prohibiting or restricting the employment of women, adolescents or children in the manufacturing process or operation;
- (c) Providing for the periodical medical examination of persons employed, or seeking to be employed, in the manufacturing process or operation, and prohibiting the employment of persons not certified as fit for such employment and requiring the payment by the occupier of the factory of fees for such medical examination;



- (d) Providing for the protection of all persons employed in the manufacturing process or operation or in the vicinity of the places where it is carried on;
- (e) Prohibiting, restricting or controlling the use of any specified materials or processes in connection with the manufacturing process or operation;
- (f) Requiring the provision of additional welfare amenities and sanitary facilities and the supply of protective equipment and clothing, and laying down the standards thereof, having regard to the dangerous nature of the manufacturing process or operation;

POWER TO PROHIBIT EMPLOYMENT ON ACCOUNT OF SERIOUS HAZARD

- (1) Where it appears to the Inspector that conditions in a factory or part thereof are such that they may cause serious hazard by way of injury or death to the persons employed therein or to the general public in the vicinity, he may, by order in writing to the occupier of the factory, state the particulars in respect of which he considers the factory or part thereof to be the cause of such serious hazard and prohibit such occupier from employing any person in the factory or any part thereof other than the minimum number of persons necessary to attend to the minimum tasks till the hazard is removed.
- (2) Any order issued by the Inspector under sub-section (1) shall have effect for a period of three days until extended by the Chief Inspector by a subsequent order.
- (3) Any person aggrieved by an order of the Inspector under sub-section (1), and the Chief Inspector under sub-section (2), shall have the right to appeal to the High Court.
- (4) Any person whose employment has been affected by an order issued under sub-section (1), shall be entitled to wages and other benefits and it shall be the duty of the occupier to provide alternative employment to him wherever possible and in the manner prescribed.
- (5) The provisions of sub-section (4) shall be without prejudice to the rights of the parties under the Industrial Disputes Act, 1947 (14 of 1947).

POWER TO PROHIBIT EMPLOYMENT ON ACCOUNT OF SERIOUS HAZARD

- (1) Where it appears to the Inspector that conditions in a factory or part thereof are such that they may cause serious hazard by way of injury or death to the persons employed therein or to the general public in the vicinity, he may, by order in writing to the occupier of the factory, state the particulars in respect of which he considers the factory or part thereof to be the cause of such serious hazard and prohibit such occupier from employing any person in the factory or any part thereof other than the minimum number of persons necessary to attend to the minimum tasks till the hazard is removed.
- (2) Any order issued by the Inspector under sub-section (1) shall have effect for a period of three days until extended by the Chief Inspector by a subsequent order.
- (3) Any person aggrieved by an order of the Inspector under sub-section (1), and the Chief Inspector under sub-section (2), shall have the right to appeal to the High Court.
- (4) Any person whose employment has been affected by an order issued under sub-section (1), shall be entitled to wages and other benefits and it shall be the duty of the occupier to provide alternative employment to him wherever possible and in the manner prescribed.
- (5) The provisions of sub-section (4) shall be without prejudice to the rights of the parties under the Industrial Disputes Act, 1947 (14 of 1947).

NOTICE OF CERTAIN DANGEROUS OCCURRENCES

Where in a factory any dangerous occurrence of such nature as may be prescribed, occurs, whether causing any bodily injury or disability or not, the manager of the factory shall send notice thereof to such authorities, and in such form and within such time, as may be prescribed.

NOTICE OF CERTAIN DISEASES

- (1) Where any worker in a factory contracts any disease specified in the Third Schedule, the manager of the factory shall send notice thereof to such Authorities, and in such form and within such time as may be prescribed.



- (2) If any medical practitioner attends on a person who is or has been employed in a factory, and who is, or is believed by the medical practitioner to be, suffering from any disease, specified in the Third Schedule the medical practitioner shall without delay send a report in writing to the office of the Chief Inspector stating—
 - (a) The name and full postal address of the patient,
 - (b) The disease from which he believes the patient to be suffering, and
 - (c) The name and address of the factory in which the patient is, or was last, employed.
- (3) Where the report under sub-section (2) is confirmed to the satisfaction of the Chief Inspector, by the certificate of a certifying surgeon or otherwise, that the person is suffering from a disease specified in the Third Schedule, he shall pay to the medical practitioner such fee as may be prescribed, and the fee so paid shall be recoverable as an arrear of land revenue from the occupier of the factory in which the person contracted the disease.
- (4) If any medical practitioner fails to comply with the provisions of sub-section (2), he shall be punishable with fine which may extend to one thousand rupees.
- (5) The Central Government may, by notification in the Official Gazette, add to or alter the Third Schedule and any such addition or alteration shall have effect as if it had been made by this Act.

POWER TO DIRECT ENQUIRY INTO CASES OF ACCIDENT OR DISEASE

- (1) The State Government may, if it considers it expedient so to do, appoint a competent person to inquire into the causes of any accident occurring in a factory or into any case where a disease specified in the Third Schedule has been, or is suspected to have been, contracted in a factory, and may also appoint one or more persons possessing legal or special knowledge to act as assessors in such inquiry.
- (2) The person appointed to hold an inquiry under this section shall have all the powers of a Civil Court under the Code of Civil Procedure, 1908 (5 of 1908), for the purposes of enforcing the attendance of witnesses and compelling the production of documents and material objects, and may also, so far as may be necessary for the purposes of the inquiry, exercise any of the powers of an Inspector under this Act; and every person required by the person making the inquiry to furnish any information shall be deemed to be legally bound so to do within the meaning of section 176 of the Indian Penal Code, 1860 (45 of 1860).
- (3) The person holding an inquiry under this section shall make a report to the State Government stating the causes of the accident, or as the case may be, disease, and any attendant circumstances, and adding any observations which he or any of the assessors may think fit to make.
- (4) The State Government may, if it thinks fit, cause to be published any report made under this section or any extracts therefrom.
- (5) The State Government may make rules for regulating the procedure as Inquiries under this section.

POWER TO TAKE SAMPLES

- (1) An Inspector may at any time during the normal working hours of a factory, after informing the occupier or manager of the factory or other person for the time being purporting to be in charge of the factory, take in the manner hereinafter provided a sufficient sample of any substance used or intended to be used in the factory, such use being—
 - (a) In the belief of the Inspector in contravention of any of the provisions of this Act or the rules made thereunder, or
 - (b) In the opinion of the Inspector likely to cause bodily injury to, or injury to the health of, workers in the factory.
- (2) Where the Inspector takes a sample under sub-section (1), he shall, in the presence of the person informed under that sub-section unless such person wilfully absents himself, divide the sample into three portions and effectively seal and suitably mark them, and shall permit such person to add his own seal and mark thereto.
- (3) The person informed as aforesaid shall, if the Inspector so requires, provide the appliances for dividing, sealing and marking the sample taken under this section.
- (4) The Inspector shall
 - (a) forthwith give one portion of the sample to the person informed under sub-section (1);
 - (b) forthwith send the second portion to a Government Analyst for analysis and report thereon;



- (c) retain the third portion for production to the Court before which proceedings, if any, are instituted in respect of the substance.
- (5) Any document purporting to be a report under the hand of any Government Analyst upon any substance submitted to him for analysis and report under this section, may be used as evidence in any proceedings instituted in respect of the substance.

SAFETY AND OCCUPATIONAL HEALTH SURVEYS

- (1) The Chief Inspector, or the Director General of Factory Advice Service and Labour Institutes, or the Director General of Health Services, to the Government of India, or such other officer as may be authorised in this behalf by the State Government or the Chief Inspector or the Director General of Factory Advice Service and Labour Institutes or the Director General of Health Services may, at any time during the normal working hours of a factory, or at any other time as is found by him to be necessary, after giving notice in writing to the occupier or manager of the factory or any other person who for the time being purports to be in charge of the factory, undertake safety and occupational health surveys and such occupier or manager or other person shall afford all facilities for such survey, including facilities for the examination and testing of plant and machinery and collection of samples and other data relevant to the survey.
- (2) For the purpose of facilitating surveys under sub-section (1) every worker shall, if so required by the person conducting the survey, present himself to undergo such medical examination as may be considered necessary by such person and furnish all information in his possession and relevant to the survey.
- (3) Any time spent by a worker for undergoing medical examination or furnishing information under sub-section (2) shall, for the purpose of calculating wages and extra wages for overtime work, be deemed to be time during which such worker worked in the factory.

Explanation : For the purposes of this section, the report, if any, submitted to the State Government by the person conducting the survey under sub-section (1) shall be deemed to be a report submitted by an Inspector under this Act.

GENERAL PENALTY FOR OFFENCES

Save as is otherwise expressly provided in this Act and subject to the provisions of section 93, if in, or in respect of, any factory there is any contravention of any of the provisions of this Act or of any rules made thereunder or of any order in writing given thereunder, the occupier and manager of the factory shall each be guilty of an offence and punishable with imprisonment for a term which may extend to two years or with fine which may extend to one lakh rupees or with both, and if the contravention is continued after conviction, with a further fine which may extend to one thousand rupees for each day on which the contravention is so continued :

Provided that where contravention of any of the provisions of Chapter IV or any rule made thereunder or under section 87 has resulted in an accident causing death or serious bodily injury, the fine shall not be less than twenty-five thousand rupees in the case of an accident causing death, and five thousand rupees in the case of an accident causing serious bodily injury. **Explanation :** In this section and in section 94 “serious bodily injury” means an injury which involves, or in all probability will involve, the permanent loss of the use of, or permanent injury to, any limb or the permanent loss of, or injury to, sight or hearing, or the fracture of any bone, but shall not include, the fracture of bone or joint (not being fracture of more than one bone or joint) of any phalanges of the hand or foot.

LIABILITY OF OWNER OF PREMISES IN CERTAIN CIRCUMSTANCES

- (1) Where in any premises separate buildings are leased to different occupiers for use as separate factories, the owner of the premises shall be responsible for the provision and maintenance of common facilities and services, such as approach roads, drainage, water supply, lighting and sanitation.
- (2) The Chief Inspector shall have, subject to the control of the State Government, power to issue orders to the owner of the premises in respect of the carrying out of the provisions of sub-section (1).
- (3) Where in any premises, independent or self-contained, floors or flats are leased to different occupiers for use as separate factories, the owner of the premises shall be liable as if he were the occupier or manager of a factory, for any contravention of the provisions of this Act in respect of—
 - (i) latrines, urinals and washing facilities in so far as the maintenance of the common supply of water for these purposes is concerned;



- (ii) fencing of machinery and plant belonging to the owner and not specifically entrusted to the custody or use of an occupier;
 - (iii) safe means of access to the floors or flats and maintenance and cleanliness of staircases and common passages;
 - (iv) precautions in case of fire;
 - (v) maintenance of hoists and lifts; and
 - (vi) maintenance of any other common facilities provided in the premises.
- (4) The Chief Inspector shall have, subject to the control of the State Government, power to issue orders to the owner of the premises in respect of the carrying out the provisions of sub-section (3).
- (5) The provisions of sub-section (3) relating to the liability of the owner shall apply where in any premises independent rooms with common latrines, urinals and washing facilities are leased to different occupiers for use as separate factories :
- Provided that the owner shall be responsible also for complying with the requirements relating to the provisions and maintenance of latrines, urinals and washing facilities.
- (6) The Chief Inspector shall have, subject to the control of the State Government, the power to issue orders to the owner of the premises referred to in sub-section (5) in respect of the carrying out of the provisions of section 46 or section 48.
- (7) Where in any premises portions of a room or a shed are leased to different occupiers for use as separate factories, the owner of the premises shall be liable for any contravention of the provisions of—
- (i) Chapter III, except sections 14 and 15;
 - (ii) Chapter IV, except sections 22, 23, 27, 34, 35 and 36 :
- Provided that in respect of the provisions of sections 21, 24 and 32 the owners liability shall be only in so far as such provisions relate to things under his control : Provided further that the occupier shall be responsible for complying with the provisions of Chapter IV in respect of plant and machinery belonging to or supplied by him;
- (iii) section 42.
- (8) The Chief Inspector shall have, subject to the control of the State Government, power to issue orders to the owner of the premises in respect of the carrying out of the provisions of sub-section (7).
- (9) In respect of sub-sections (5) and (7), while computing for the purposes of any of the provisions of this Act the total number of workers employed, the whole of the premises shall be deemed to be a single factory.

ENHANCED PENALTY AFTER PREVIOUS CONVICTION

- (1) If any person who has been convicted of any offence punishable under section 92 is again guilty of an offence involving a contravention of the same provision, he shall be punishable on a subsequent conviction with imprisonment for a term which may extend to three years or with fine which shall not less than ten thousand rupees but which may extend to two lakh rupees or with both :

Provided that the court may, for any adequate and special reasons to be mentioned in the judgment, impose a fine of less than ten thousand rupees:

Provided further that where contravention of any of the provisions of Chapter IV or any rule made thereunder or under section 87 has resulted in an accident causing death or serious bodily injury, the fine shall not be less than thirty five thousand rupees in the case of an accident causing death and ten thousand rupees in the case of an accident causing serious bodily injury.

- (2) For the purposes of sub-section (1), no cognizance shall be taken of any conviction made more than two years before the commission of the offence for which the person is subsequently being convicted.

PENALTY FOR OBSTRUCTING INSPECTOR

Whoever wilfully obstructs an Inspector in the exercise of any power conferred on him by or under this Act, or fails to produce on demand by an Inspector any registers or other documents in his custody kept in pursuance of this Act or of any rules made thereunder, or conceals or prevents any worker in a factory from appearing before, or being examined by, an Inspector, shall be punishable with imprisonment for a term which may extend to six months or with fine which may extend to ten thousand rupees or with both.



PENALTY FOR WRONGFULLY DISCLOSING RESULTS OF ANALYSIS UNDER SECTION 91

Whoever, except in so far as it may be necessary for the purposes of a prosecution for any offence punishable under this Act, publishes or discloses to any person the results of an analysis made under section 91, shall be punishable with imprisonment for a term which may extend to six months or with fine which may extend to ten thousand rupees or with both.

PENALTY FOR CONTRAVENTION OF THE PROVISIONS OF SECTIONS 41B, 41C AND 41H

- (1) Whoever fails to comply with or contravenes any of the provisions of section 41B, 41C or 41H or the rules made thereunder, shall, in respect of such failure or contravention, be punishable with imprisonment for a term which may extend to seven years and with fine which may extend to two lakh rupees, and in case the failure or contravention continues, with additional fine which may extend to five thousand rupees for every day during which such failure or contravention continues after the conviction for the first such failure or contravention.
- (2) If the failure or contravention referred to in sub-section (1) continues beyond a period of one year after the date of conviction, the offender shall be punishable with imprisonment for a term which may extend to ten years.

OFFENCES BY WORKERS

- (1) Subject to the provisions of section 111, if any worker employed in a factory contravenes any provision of this Act or any rules or orders made thereunder, imposing any duty or liability on workers, he shall be punishable with fine which may extend to five hundred rupees.
- (2) Where a worker is convicted of an offence punishable under sub-section (1), the occupier or manager of the factory shall not be deemed to be guilty of an offence in respect of that contravention, unless it is proved that he failed to take all reasonable measures for its prevention.

PENALTY FOR USING FALSE CERTIFICATE OF FITNESS

Whoever knowingly uses or attempts to use, as a certificate of fitness granted to himself under section 70, a certificate granted to another person under that section, or who, having procured such a certificate, knowingly allows it to be used, or an attempt to use to be made, by another person, shall be punishable with imprisonment for a term which may extend to two months or with fine which may extend to one thousand rupees or with both.

PENALTY FOR PERMITTING DOUBLE EMPLOYMENT OF CHILD

If a child works in a factory on any day on which he has already been working in another factory, the parent or guardian of the child or the person having custody of or control over him or obtaining any direct benefit from his wages, shall be punishable with fine which may extend to one thousand rupees unless it appears to the Court that the child so worked without the consent or connivance of such parent, guardian or person.

EXEMPTION OF OCCUPIER OR MANAGER FROM LIABILITY IN CERTAIN CASES

Where the occupier or manager of a factory is charged with an offence punishable under this Act, he shall be entitled, upon complaint duly made by him and on giving to the prosecutor not less than three clear days notice in writing of his intention so to do, to have any other person whom he charges as the actual offender brought before the Court at the time appointed for hearing the charge; and if, after the commission of the offence has been proved, the occupier or manager of the factory, as the case may be, proves to the satisfaction of the court—

- (a) that he has used due diligence to enforce the execution of this Act, and
- (b) that the said other person committed the offence in question without his knowledge, consent or connivance, - that other person shall be convicted of the offence and shall be liable to the like punishment as if he were the occupier or manager of the factory, and the occupier or manager, as the case may be, shall be discharged from any liability under this Act in respect of such offence : Provided that in seeking to prove as aforesaid, the occupier or manager of the factory, as the case may be, may be examined on oath, and his evidence and that of any witness whom he calls in his support shall be subject to cross-examination on behalf of the person he charges as the actual offender and by the prosecutor : Provided further that, if the person charged as the actual offender by the occupier or manager cannot be brought before the Court at the time appointed for hearing the charge, the Court shall adjourn the hearing from time to time for a period not exceeding three months and if by the end of the said period the person charged as the actual offender cannot still be brought before the Court, the Court shall proceed to hear the charge against the occupier or manager and shall, if the offence be proved, convict the occupier or manager.

**POWER OF COURT TO MAKE ORDERS**

- (1) Where the occupier or manager of a factory is convicted of an offence punishable under this Act the Court may, in addition to awarding any punishment, by order in writing require him, within a period specified in the order (which the Court may, if it thinks fit and on application in such behalf, from time to time extend) to take such measures as may be so specified for remedying the matters in respect of which the offence was committed.
- (2) Where an order is made under sub-section (1), the occupier or manager of the factory, as the case may be, shall not be liable under this Act in respect of the continuation of the offence during the period or extended period, if any, allowed by the Court, but if, on the expiry of such period or extended period, as the case may be, the order of the Court has not been fully complied with, the occupier or manager, as the case may be, shall be deemed to have committed a further offence, and may be sentenced therefor by the Court to undergo imprisonment for a term which may extend to six months or to pay a fine which may extend to one hundred rupees for every day after such expiry on which the order has not been complied with, or both to undergo such imprisonment and to pay such fine, as aforesaid.

PRESUMPTION AS TO EMPLOYMENT

If a person is found in a factory at any time, except during intervals for meals or rest, when work is going on or the machinery is in motion, he shall until the contrary is proved, be deemed for the purposes of this Act and the rules made thereunder to have been at that time employed in the factory.

ONUS AS TO AGE

- (1) When any act or omission would, if a person were under a certain age, be an offence punishable under this Act, and such person is in the opinion of the Court *prima facie* under such age, the burden shall be on the accused to prove that such person is not under such age.
- (2) A declaration in writing by a certifying surgeon relating to a worker that he has personally examined him and believes him to be under the age stated in such declaration shall, for the purposes of this Act and the rules made thereunder, be admissible as evidence of the age of that worker.

ONUS OF PROVING LIMITS OF WHAT IS PRACTICABLE, ETC

In any proceeding for an offence for the contravention of any provision of this Act or rules made thereunder consisting of a failure to comply with a duty or requirement to do something, it shall be for the person who is alleged to have failed to comply with such duty or requirement, to prove that it was not reasonably practicable, or, as the case may be, all practicable measures were taken to satisfy the duty or requirement.

COGNIZANCE OF OFFENCES

- (1) No Court shall take cognizance of any offence under this Act except on complaint by, or with the previous sanction in writing of, an Inspector.
- (2) No Court below that of a Presidency Magistrate or of a Magistrate of the first class shall try any offence punishable under this Act.

LIMITATION OF PROSECUTIONS

No Court shall take cognizance of any offence punishable under this Act unless complaint thereof is made within three months of the date on which the alleged commission of the offence came to the knowledge of an Inspector :

Provided that where the offence consists of disobeying a written order made by an Inspector, complaint thereof may be made within six months of the date on which the offence is alleged to have been committed.

Explanation : For the purposes of this section,—

- (a) In the case of a continuing offence, the period of limitation shall be computed with reference to every point of time during which the offence continues;
- (b) Where for the performance of any act time, is granted or extended on an application made by the occupier or manager of a factory, the period of limitation shall be computed from the date on which the time so granted or extended, expired.



JURISDICTION OF A COURT FOR ENTERTAINING PROCEED-INGS, ETC., FOR OFFENCE

For the purposes of conferring jurisdiction on any court in relation to an offence under this Act or the rules made thereunder in connection with the operation of any plant, the place where the plant is for the time being situate shall be deemed to be the place where such offence has been committed.

APPEALS

- (1) The manager of a factory on whom an order in writing by an Inspector has been served under the provisions of this Act or the occupier of the factory may, within thirty days of the service of the order, appeal against it to the prescribed authority, and such authority may, subject to rules made in this behalf by the State Government, confirm, modify or reverse the order.
- (2) Subject to rules made in this behalf by the State Government (which may prescribe classes of appeals which shall not be heard with the aid of assessors), the appellate authority may, or if so required in the petition of appeal shall, hear the appeal with the aid of assessors, one of whom shall be appointed by the appellate authority and the other by such body representing the industry concerned as may be prescribed :
Provided that if no assessor is appointed by such body before the time fixed for hearing the appeal, or if the assessor so appointed fails to attend the hearing at such time, the appellate authority may, unless satisfied that the failure to attend is due to sufficient cause, proceed to hear the appeal without the aid of such assessor or, if it thinks fit, without the aid of any assessor.
- (3) Subject to such rules as the State Government may make in this behalf and subject to such conditions as to partial compliance or the adoption of temporary measures as the appellate authority may in any case think fit to impose, the appellate authority may, if it thinks fit, suspend the order appealed against pending the decision of the appeal.

DISPLAY OF NOTICES

- (1) In addition to the notices required to be displayed in any factory by or under this Act, there shall be displayed in every factory a notice containing such abstracts of this Act and of the rules made thereunder as may be prescribed and also the name and address of the Inspector and the certifying surgeon.
- (2) All notices required by or under this Act to be displayed in a factory shall be in English and in a language understood by the majority of the workers in the factory, and shall be displayed at some conspicuous and convenient place at or near the main entrance to the factory, and shall be maintained in a clean and legible condition.
- (3) The Chief Inspector may, by order in writing served on the manager of any factory, require that there shall be displayed in the factory any other notice or poster relating to the health, safety or welfare of the workers in the factory.

SERVICE OF NOTICE

The State Government may make rules prescribing the manner of the service of orders under this Act on owners, occupiers or managers of factories.

RETURNS

The State Government may make rules requiring owners, occupiers or managers of factories to submit such returns, occasional or periodical, as may in its opinion be required for the purposes of this Act.

OBLIGATIONS OF WORKERS

- (1) No worker in a factory—
 - (a) Shall wilfully interfere with or misuse any appliance, convenience or other thing provided in a factory for the purposes of securing the health, safety or welfare of the workers therein;
 - (b) Shall wilfully and without reasonable cause do anything likely to endanger himself or others; and
 - (c) Shall wilfully neglect to make use of any appliance or other thing provided in the factory for the purposes of securing the health or safety of the workers therein.
- (2) If any worker employed in a factory contravenes any of the provisions of this section or of any rule or order made thereunder, he shall be punishable with imprisonment for a term which may extend to three months, or with fine which may extend to one hundred rupees, or with both.

**RIGHT OF WORKERS, ETC**

Every worker shall have the right to—

- (i) Obtain from the occupier, information relating to workers' health and safety at work;
- (ii) Get trained within the factory wherever possible, or, to get himself sponsored by the occupier for getting trained at a training centre or institute, duly approved by the Chief Inspector, where training is imparted for workers' health and safety at work;
- (iii) Represent to the Inspector directly or through his representative in the matter of inadequate provision for protection of his health or safety in the factory.

GENERAL POWER TO MAKE RULES

The State Government may make rules providing for any matter which, under any of the provisions of this Act, is to be or may be prescribed or which may be considered expedient in order to give effect to the purposes of this Act.

POWERS OF CENTRE TO GIVE DIRECTIONS

The Central Government may give directions to a State Government as to the carrying into execution of the provisions of this Act.

NO CHARGE FOR FACILITIES AND CONVENIENCES

Subject to the provisions of section 46 no fee or charge shall be realised from any worker in respect of any arrangements or facilities to be provided, or any equipments or appliances to be supplied by the occupier under the provisions of this Act.

PUBLICATION OF RULES

- (1) All rules made under this Act shall be published in the Official Gazette, and shall be subject to the condition of previous publication; and the date to be specified under clause (3) of section 23 of the General Clauses Act, 1897 (10 of 1897), shall be not less than forty-five days from the date on which the draft of the proposed rules was published.
- (2) Every rule made by the State Government under this Act shall be laid, as soon as may be after it is made, before the State Legislature.

APPLICATION OF ACT TO GOVERNMENT FACTORIES

Unless otherwise provided, this Act shall apply to factories belonging to the Central or any State Government.

PROTECTION TO PERSONS ACTING UNDER THIS ACT

No suit, prosecution or other legal proceeding shall lie against any person for anything which is in good faith done or intended to be done under this Act.

RESTRICTION ON DISCLOSURE OF INFORMATION (Sec. 118)

- (1) No Inspector shall, while in service or after leaving the service, disclose otherwise than in connection with the execution, or for the purposes, of this Act any information relating to any manufacturing or commercial business or any working process which may come to his knowledge in the course of his official duties.
- (2) Nothing in sub-section (1) shall apply to any disclosure of information made with the previous consent in writing of the owner of such business or process or for the purposes of any legal proceeding (including arbitration) pursuant to this Act or of any criminal proceeding which may be taken, whether pursuant to this Act or otherwise, or for the purpose of any report of such proceedings as aforesaid.
- (3) If any Inspector contravenes the provisions of sub-section (1) he shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both.

RESTRICTION ON DISCLOSURE OF INFORMATION (Sec. 118A)

- (1) Every Inspector shall treat as confidential the source of any complaint brought to his notice on the breach of any provision of this Act.
- (2) No inspector shall, while making an inspection under this Act, disclose to the occupier, manager or his representative that the inspection is made in pursuance of the receipt of a complaint : Provided that nothing in this sub-section shall apply to any case in which the person who has made the complaint has consented to disclose his name.



3.2 THE INDUSTRIAL DISPUTES ACT, 1947

INTRODUCTION

Prior to the year 1947, industrial disputes were being settled under the provisions of the Trade Disputes Act, 1929. Experience of the working of the 1929 Act revealed various defects which needed to be overcome by a fresh legislation. Accordingly the Industrial Disputes Bill was introduced in the Legislature. The Bill was referred to the select committee. On the recommendations of the Select Committee amendments were made in the original Bill.

STATEMENT OF OBJECTS AND REASONS

Experience of the working of the Trade Disputes Act, 1929, has revealed that its main defect is that, while restraints have been imposed on the rights of strike and lock-out in public utility services, no provision has been made to render the proceedings institutable under the Act for the settlement of an industrial dispute, either by reference to a Board of Conciliation or to a Court of Inquiry, conclusive and binding on the parties to the dispute. This defect was overcome during the war by empowering under Rule 81A of the Defence of India, Rules, the Central Government to refer industrial disputes to adjudicators and to enforce their awards. Rule 81A, which was to lapse on the 1st October, 1946, is being kept in force by the Emergency Powers (Continuance).

Ordinance, 1946, for a further period of six months; and as industrial unrest in checking which this rule has proved useful, is gaining momentum due to the stress of post industrial re-adjustment, the need of permanent legislation in replacement of this rule is self-evident. This Bill embodies the essential principles of Rule 81A, which have proved generally acceptable to both employers and workmen, retaining intact, for the most part, the provisions of the Trade Disputes Act, 1929.

The two institutions for the prevention and settlement of industrial disputes provided for in the Bill are the Works Committees consisting of representatives of employers and workmen, Industrial Tribunal consisting of one or more members possessing qualifications ordinarily required for appointment as Judge of a High Court. Power has been given to appropriate Government to require Works Committees to be constituted in every industrial establishment employing 100 workmen, or more and their duties will be to remove causes of friction between the employer and workmen in the day-to-day working of the establishment and to promote measures for securing amity and good relations between them. Industrial peace will be most enduring where it is founded on voluntary settlement, and it is hoped that the Works Committees will render recourse to the remaining machinery provided for in the Bill for the settlements of disputes infrequent. A reference to an Industrial Tribunal will lie where both the parties to an industrial dispute apply for such reference and also where the appropriate Government considers it expedient so to do. An award of a Tribunal may be enforced either wholly or in part by the appropriate Government for a period not exceeding one year. The power to refer disputes to Industrial Tribunals and enforce their awards is an essential corollary to the obligation that lies on the Government to secure conclusive determination of the disputes with a view to redressing the legitimate grievances of the parties thereto, such obligation arising from the imposition of restraints on the rights of strike and lock-out, which must remain inviolate, except where considerations of public interest override such rights.

The Bill also seeks to re-orient the administration of the conciliation machinery provided in the Trade Disputes Act. Conciliation will be compulsory in all disputes in public utility services and optional in the case of other industrial establishments. With a view to expedite conciliation proceedings time limits have been prescribed for conclusion thereof 14 days in the case of conciliation officers and two months in the case of Board of Conciliation from the date of notice of strike. A settlement arrived at in the course of conciliation proceedings will be binding for such period as may be agreed upon by the parties and where no period has been agreed upon, for a period of one year, and will continue to be binding until revoked by a 3 month's notice by either party to the dispute.

Another important new feature of the Bill relates to the prohibition of strikes and lock-outs during the pendency of conciliation and adjudication proceedings of settlements reached in the course of conciliation proceedings and of awards of Industrial Tribunals declared binding by the appropriate Government. The underlying argument is that where a dispute has been referred to conciliation for adjudication a strike or lock-out, in furtherance thereof, is both unnecessary and inexpedient. Where, on the date of reference to



conciliation or adjudication a strike or lock-out is already in existence, power is given to the appropriate Government to prohibit its continuance lest the chances of settlement or speedy determination of the dispute should be jeopardized.

The Bill also empowers the appropriate Government to declare, if public interest or emergency so requires, by notification in the Official Gazette, any industry to be a public utility service, for such period, if any, as may be specified in the notification.

ACT 14 OF 1947

The Industrial Disputes Bill having been passed by the Legislature received its assent on 11th March, 1947. It came into force on first day of April, 1947 as THE INDUSTRIAL DISPUTES ACT, 1947 (14 of 1947).

PRELIMINARY

Objectives of the Act :-

The main objectives of the Act are as follows:

- (i) Securing industrial peace through-
 - (a) preventing and settling industrial disputes between employers and employees.
 - (b) setting up an internal Works Committee for maintaining good relations between employers and employees.
 - (c) promoting good relations through external machineries like Conciliation, Courts of Enquiry, Industrial Tribunals, National Tribunals and Labour Courts.
- (ii) Ameliorating the condition of workmen in industry
 - (a) by redressing the grievances of workmen through a statutory machinery.
 - (b) by assuring job security.

1. EXTENT

- (1) This Act may be called the Industrial Disputes Act, 1947.
- (2) It extends to the whole of India.
- (3) It shall come into force on the first day of April, 1947.

2. BASIC CONCEPTS

In this Act, unless there is anything repugnant in the subject or context,

- (a) “**appropriate Government**” means [Sec 2(a)]
 - (i) in relation to any industrial dispute concerning any industry carried on by or under the authority of the Central Government,
 - (ii) or, by a railway company or concerning any such controlled industry as may be specified in this behalf by the Central Government;
 - (iii) or, in relation to an industrial dispute concerning 'a Dock Labour Board established under section 5A of the Dock Workers (Regulation of Employment) Act,(9 of 1948),
 - (iv) or, 'the Industrial Finance Corporation of India Limited formed and registered under the Companies Act, 1956 (1 of 1956),
 - (v) or, the Employees' State Insurance Corporation established under section 3 of the Employees' State Insurance Act, 1948 (34 of 1948);
 - (vi) or, the Board of Trustees constituted under section 3A of the Coal Mines Provident Fund and Miscellaneous Provisions Act, 1948 (46 of 1948), or the Central Board of Trustees and the State Boards of Trustees constituted under section 5A and section 5B, respectively, of the Employees' Provident Fund and Miscellaneous Provisions Act, 1952 (19 of 1952),
 - (vii) or, the Life Insurance Corporation of India established under section 3 of the Life Insurance Corporation Act, 1956 (31 of 1956),
 - (viii) or, the Oil and Natural Gas Corporation Limited registered under the Companies Act, 1956 (1 of 1956);



- (ix) or, the Deposit Insurance and Credit Guarantee Corporation established under section 3 of the Deposit Insurance and Credit Guarantee Corporation Act, 1961 (47 of 1961), or the Central Warehousing Corporation established under section 3 of the Warehousing Corporations Act, 1962 (58 of 1962);
- (x) or, the Unit Trust of India established under section 3 of the Unit Trust of India Act, 1963 (52 of 1963);
- (xi) or the Food Corporation of India established under section 3;
- (xii) or a Board of Management established for two or more contiguous States under section 16, of the Food Corporations Act, 1964 (37 of 1964);
- (xiii) or the Airports Authority of India constituted under section 3 of the Airports Authority of India Act, 1994 (55 of 1994);
- (xiv) or a Regional Rural Bank established under section 3 of the Regional Rural Banks Act, 1976 (21 of 1976);
- (xv) or the Export Credit and Guarantee Corporation Limited or the Industrial Reconstruction Bank of India Limited, the National Housing Bank established under section 3 of the National Housing Bank Act, 1987 (53 of 1987);
- (xvi) or an air transport service, or a banking or an insurance company, a mine, an oil field, a Cantonment Board, or a major port, the Central Government, and
- (xvii) in relation to any other industrial dispute, the State Government :
- (aa) “**arbitrator**” includes an umpire;
- (aaa) “**average pay**” means the average of the wages payable to a workman :
 - (i) in the case of monthly paid workman, in the three complete calendar months,
 - (ii) in the case of weekly paid workman, in the four complete weeks,
 - (iii) in the case of daily paid workman, in the twelve full working days, preceding the date on which the average pay becomes payable if the workman had worked for three complete calendar months or four complete weeks or twelve full working days, as the case may be, and where such calculation cannot be made, the average pay shall be calculated as the average of the wages payable to a workman during the period he actually worked;
- Sec 2(b) “**award**” means an interim or a final determination of any industrial dispute or of any question relating thereto by any Labour Court, Industrial Tribunal or National Industrial Tribunal and includes an arbitration award made under section 10A;
- Sec 2(bb) “**banking company**” means a banking company as defined in section 5 of the Banking Companies Act, 1949 (10 of 1949), having branches or other establishments in more than one State, and includes the Export - Import Bank of India the Industrial Reconstruction Bank of India, the Industrial Development Bank of India, the Small Industries Development Bank of India established under section 3 of the Small Industries Development Bank of India Act, 1989, the Reserve Bank of India, the State Bank of India, a corresponding new bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (5 of 1970) a corresponding new bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 (40 of 1980), and any subsidiary bank, as defined in the State Bank of India (Subsidiary Banks) Act, 1959 (38 of 1959);
- Sec 2(c) “**Board**” means a Board of Conciliation constituted under this Act;
- (cc) “**closure**” means the permanent closing down of a place of employment or part thereof;
- (d) “**conciliation officer**” means a conciliation officer appointed under this Act;
- (e) “**conciliation proceeding**” means any proceeding held by a conciliation officer or Board under this Act;
- (ee) “**controlled industry**” means any industry the control of which by the Union has been declared by any Central Act to be expedient in the public interest;
- (f) “**Court**” means a Court of Inquiry constituted under this Act;



(g) “**employer**” means:

(i) in relation to any industry carried on by or under the Authority of any department of the Central Government or a State Government, the Authority prescribed in this behalf, or where no Authority is prescribed, the head of the department;

(ii) in relation to an industry carried on by or on behalf of a local Authority, the Chief Executive Officer of that Authority;

(h) “**executive**”, in relation to a trade union, means the body, by whatever name called, to which the management of the affairs of the trade union is entrusted;

(i) a person shall be deemed to be “**independent**” for the purpose of his appointment as the Chairman or other member of a Board, Court or Tribunal, if he is unconnected with the industrial dispute referred to such Board, Court or Tribunal or with any industry directly affected by such dispute: Provided that no person shall cease to be independent by reason only of the fact that he is a shareholder of an incorporated company which is connected with, or likely to be affected by, such industrial dispute; but in such a case, he shall disclose to the appropriate Government the nature and extent of the shares held by him in such company;

(j) “**industry**” means any business, trade, undertaking, manufacture or calling of employers and includes any calling, service, employment, handicraft, or industrial occupation or avocation of workmen;

The term ‘industry’ does not include-

(i) Agricultural operations

(ii) Hospitals / dispensaries

(iii) Educational, scientific, research or training institutions

(iv) Organisations engaged in charitable, social or philanthropic work

(v) Khadi/Village industries

(vi) Any activity of Government relatable to sovereign functions of Govt.

(vii) Domestic service

(viii) Any professional activity, provided the number of persons employed is less than ten

(ix) Any activity carried out by co-operative society, club or any other body of individuals , if total number of persons employed is less than ten.

(k) “**industrial dispute**” means any dispute or difference between employers and employees, or between employers and workmen, or between workmen and workmen, which is connected with the employment or non-employment or the terms of employment or with the conditions of labour, of any persons;

(ka) “Industrial establishment or undertaking” means an establishment or undertaking in which any industry is carried on :

Provided that where several activities are carried on in an establishment or undertaking and only one or some of such activities is or are an industry or industries, then (a) if any unit of such establishment or undertaking carrying on any activity, being an industry, is severable from the other unit or units of such establishment or undertaking, such unit shall be deemed to be a separate industrial establishment or undertaking. (b) If the predominant activity or each of the predominant activities carried on in such establishment or undertaking or any unit thereof in an industry and the other activity or each of the other activities carried on in such establishment or undertaking or unit thereof is not severable from and is, for the purpose of carrying on, or aiding the carrying on of, such predominant activity or activities, the entire establishment or undertaking or, as the case may be, unit thereof shall be deemed to be an industrial establishment or undertaking.

Lay-off [Sec. 2(kkk)] - means failure, refusal or inability of an employer to give employment to a workman (a) whose name is borne on the muster -rolls of his industrial establishment, and (b) who has not been retrenched. The failure, refusal or inability of an employer to give employment may be due to- (1) shortage of coal, power, or raw materials, (2) the accumulation of stocks (3) breakdown of machinery (4) natural calamity or any other connected reasons.



Lock-out [sec 2(l)] - It means **temporary** closing of a place of employment ,or suspension of work or refusal by employer to continue to employ any number of persons employed by him. It may be said that lock-out is a weapon in hands of employer.

Retrenchment [sec.2(oo)] - It means termination of service of a workman by an employer for any reason whatsoever, otherwise than as punishment inflicted as a part of disciplinary action. Retrenchment doesnot include:

- (i) VRS
- (ii) Retirement on reaching superannuation
- (iii) Termination of service on ground of ill-health

Strike [sec.2(q)] It means-

- (i) a cessation of work by a body of persons employed in any industry acting in combination ;or
- (ii) a concerted refusal of any number of persons who are or have been so employed to continue work or accept employment;or
- (iii) refusal under a common understanding of any number of such persons to continue work or accept employment.

Settlement[sec2(p)] It means-

- (i) a settlement arrived at in the course of conciliation proceedings (which may be held by a conciliation officer or Board of Conciliation) and includes,
- (ii) a written agreement between the employer and workmen arrived at otherwise than in the course of conciliation proceeding where such agreement has been signed by parties thereto in such a manner as may be prescribed and a copy thereof has been sent to an officer authorized in this behalf by an appropriate Government and the Conciliation Officer.

Unfair labour practice [sec.2(ra)] It means any of the practices specified in the Fifth Schedule (introduced by Amendment Act of 1982) which declares certain labour practices as unfair on the part of employers and their trade unions and on the part of workmen and their trade union.

Industrial Dispute may be Individual Dispute

Where any employer discharges, dismisses, retrenches or otherwise terminates the services of an individual workman, any dispute or difference between that workman and his employer connected with, or arising out of, such discharge, dismissal, retrenchment or termination shall be deemed to be an industrial dispute notwithstanding that no other workman nor any union of workmen is a party to the dispute. [Sec 2A]

Collective dispute may relate to the following :

- (i) Wages, bonus, gratuity and other allowances.
- (ii) Duration of working hours, leave, holidays etc.
- (iii) Rules governing discipline, retrenchment, closure, rationalization.

All collective disputes are industrial disputes.

AUTHORITIES UNDER THIS ACT

1. WORKS COMMITTEE (Sec 3)

- (1) In the case of any industrial establishment in which one hundred or more workmen are employed or have been employed on any day in the preceding twelve months, the appropriate Government may by general or special order require the employer to constitute in the prescribed manner a Works Committee consisting of representatives of employers and workmen engaged in the establishment so however that the number of representatives of workmen on the Committee shall not be less than the number of representatives of the employer. The representatives of the workmen shall be chosen in the prescribed manner from among the workmen engaged in the establishment and in consultation with their trade union, if any, registered under the Indian Trade Unions Act, 1926 (16 of 1926).
- (2) It shall be the duty of the Works Committee to promote measures for securing and preserving amity and good relations between the employer and workmen and, to that end, to comment upon matters



of their common interest or concern and endeavour to compose any material difference of opinion in respect of such matters.

2. CONCILIATION OFFICERS (Sec 4)

- (1) The appropriate Government may, by notification in the Official Gazette, appoint such number of persons as it thinks fit, to be conciliation officers, charged with the duty of mediating in and promoting the settlement of industrial disputes.
- (2) A conciliation officer may be appointed for a specified area or for specified industries in a specified area or for one or more specified industries and either permanently or for a limited period.

3. BOARDS OF CONCILIATION (Sec 5)

- (1) The appropriate Government may as occasion arises, by notification in the Official Gazette, constitute a Board of Conciliation for promoting the settlement of an industrial dispute.
- (2) A Board shall consist of a chairman and two or four other members, as the appropriate Government thinks fit.
- (3) The chairman shall be an independent person and the other members shall be persons appointed in equal numbers to represent the parties to the dispute and any person appointed to represent a party shall be appointed on the recommendation of that party:
Provided that, if any party fails to make a recommendation as aforesaid within the prescribed time, the appropriate Government shall appoint such persons as it thinks fit to represent that party.
- (4) A Board, having the prescribed quorum, may act notwithstanding the absence of the chairman or any of its members or any vacancy in its number:
Provided that if the appropriate Government notifies the Board that the services of the chairman or of any other member have ceased to be available, the Board shall not act until a new chairman or member, as the case may be, has been appointed.

4. COURTS OF INQUIRY (Sec 6)

- (1) The appropriate Government may as occasion arises by notification in the Official Gazette constitute a Court of Inquiry for inquiring into any matter appearing to be connected with or relevant to an industrial dispute.
- (2) A court may consist of one independent person or of such number of independent persons as the appropriate Government may think fit and where a court consists of two or more members, one of them shall be appointed as the chairman.
- (3) A court, having the prescribed quorum, may act notwithstanding the absence of the chairman or any of its members or any vacancy in its number:
Provided that, if the appropriate Government notifies the court that the services of the chairman have ceased to be available, the court shall not act until a new chairman has been appointed.

5. LABOUR COURTS (Sec 7)

- (1) The appropriate Government may, by notification in the Official Gazette, constitute one or more Labour Courts for the adjudication of industrial disputes relating to any matter specified in the Second Schedule and for performing such other functions as may be assigned to them under this Act.
- (2) A Labour Court shall consist of one person only to be appointed by the appropriate Government.
- (3) A person shall not be qualified for appointment as the presiding officer of a Labour Court, unless -
 - (a) he is, or has been, a Judge of a High Court; or
 - (b) he has, for a period of not less than three years, been a District Judge or an Additional District Judge; or
 - (d) he has held any judicial office in India for not less than seven years; or
 - (e) he has been the presiding officer of a Labour Court constituted under any Provincial Act or State Act for not less than five years.



COMMENTS

This section relates to the constitution of the Labour Court for adjudication of industrial disputes relating to any matter specified in the Second Schedule; *Jagdish Narain Sharma v. Rajasthan Patrika Ltd.*, 1994 LLR 265 (Raj).

6. INDUSTRIAL TRIBUNALS (Sec 7A)

- (1) The appropriate Government may, by notification in the Official Gazette, constitute one or more Industrial Tribunals for the adjudication of industrial disputes relating to any matter, whether specified in the Second Schedule or the Third Schedule and for performing such other functions as may be assigned to them under this Act.
- (2) A Tribunal shall consist of one person only to be appointed by the appropriate Government.
- (3) A person shall not be qualified for appointment as the presiding officer of a Tribunal unless:
 - (a) he is, or has been, a Judge of a High Court; or
 - (aa) he has, for a period of not less than three-years, been a District Judge or an Additional District Judge;
- (4) The appropriate Government may, if it so thinks fit, appoint two persons as assessors to advise the Tribunal in the proceeding before it.

COMMENTS

Section 7A empowers the appropriate Government to constitute one or more Industrial Tribunals for adjudication of the disputes relating to any matter specified in the Schedules. The Second Schedule enumerates the matters which fall within the jurisdiction of the Labour Court. The Third Schedule enumerates the matters which fall within the jurisdiction of the Industrial Tribunal; *Jagdish Narain Sharma v. Rajasthan Patrika Ltd.*, 1994 LLR 265 (Raj).

7. NATIONAL TRIBUNALS (Sec 7B)

- (1) The Central Government may, by notification in the Official Gazette, constitute one or more National Industrial Tribunals for the adjudication of industrial disputes which, in the opinion of the Central Government, involve questions of national importance or are of such a nature that industrial establishments situated in more than one State are likely to be interested in, or affected by, such disputes.
- (2) A National Tribunal shall consist of one person only to be appointed by the Central Government.
- (3) A person shall not be qualified for appointment as the presiding officer of a National Tribunal unless he is, or has been, a judge of a High Court.
- (4) The Central Government may, if it so thinks fit, appoint two persons as assessors to advise the National Tribunal in the proceeding before it.

DISQUALIFICATIONS FOR THE PRESIDING OFFICERS OF LABOUR COURTS, TRIBUNALS AND NATIONAL TRIBUNALS (Sec 7C)

No person shall be appointed to, or continue in, the office of the presiding officer of a Labour Court, Tribunal or National Tribunal, if—

- (a) he is not an independent person; or
- (b) he has attained the age of sixty-five years.

FILLING OF VACANCIES (Sec 8)

If, for any reason a vacancy (other than a temporary absence) occurs in the office of the presiding officer of a Labour Court, Tribunal or National Tribunal or in the office of the Chairman or any other member of a Board or court, then, in the case of a National Tribunal, the Central Government and in any other case, the appropriate Government, shall appoint another person in accordance with the provisions of this Act to fill the vacancy, and the proceeding may be continued before the Labour Court, Tribunal, National Tribunal, Board or Court, as the case may be, from the stage at which the vacancy is filled.

**FINALITY OF ORDERS CONSTITUTING BOARDS, ETC (Sec 9)**

- (1) No order of the appropriate Government or of the Central Government appointing any person as the Chairman or any other member of a Board or Court or as the presiding officer of a Labour Court, Tribunal or National Tribunal shall be called in question in any manner; and no act or proceeding before any Board or Court shall be called in question in any manner on the ground merely of the existence of any vacancy in, or defect in the constitution of, such Board or Court.
- (2) No settlement arrived at in the course of a conciliation proceeding shall be invalid by reason only of the fact that such settlement was arrived at after the expiry of the period referred to in sub-section (6) of section 12 or sub-section (5) of section 13, as the case may be.
- (3) Where the report of any settlement arrived at in the course of conciliation proceeding before a Board is signed by the chairman and all the other members of the Board, no such settlement shall be invalid by reason only of the casual or unforeseen absence of any of the members (including the Chairman) of the Board during any stage of the proceeding.

NOTICE OF CHANGE (Sec 9A)

No, employer, who proposes to effect any change in the conditions of service applicable to any workman in respect of any matter specified in the Fourth Schedule, shall effect such change,

- (a) without giving to the workmen likely to be affected by such change a notice in the prescribed manner of the nature of the change proposed to be effected; or
- (b) within twenty-one days of giving such notice:

Provided that no notice shall be required for effecting any such change—

- (a) where the change is effected in pursuance of any settlement or award; or
- (b) where the workmen likely to be affected by the change are persons to whom the Fundamentals and Supplementary Rules, Civil Services (Classification, Control and Appeal) Rules, Civil Services (Temporary Service) Rules, Revised Leave rules, Civil Service Regulations, Civilians in Defence Services (Classification, Control and Appeal) Rules or the Indian Railway Establishment Code or any other rules or regulations that may be notified in this behalf by the appropriate Government in the official Gazette, apply.

POWER OF GOVERNMENT TO EXEMPT (Sec 9B)

Where the appropriate Government is of opinion that the application of the provisions of section 9A to any class of industrial establishments or to any class of workmen employed in any industrial establishment affect the employers in relation thereto so prejudicially that such application may cause serious repercussion on the industry concerned and that public interest so requires, the appropriate Government may, by notification in the Official Gazette, direct that the provisions of the said section shall not apply or shall apply, subject to such conditions as may be specified in the notification, to that class of industrial establishments or to that class of workmen employed in any industrial establishment.

REFERENCE OF DISPUTES TO BOARDS, COURTS OR TRIBUNALS (Sec 10)

- (1) Where the appropriate Government is of opinion that any industrial dispute exists or is apprehended, it may at any time, by order in writing :
 - (a) Refer the dispute to a Board for promoting a settlement thereof; or
 - (b) Refer any matter appearing to be connected with or relevant to the dispute to a court for inquiry; or
 - (c) Refer the dispute or any matter appearing to be connected with, or relevant to, the dispute, if it relates to any matter specified in the Second Schedule, to a Labour court for adjudication; or
 - (d) Refer the dispute or any matter appearing to be connected with, or relevant to, the dispute, whether it relates to any matter specified in the Second Schedule or the Third Schedule, to a Tribunal for adjudication :

Provided that where the dispute relates to any matter specified in the Third Schedule and is not likely to affect more than one hundred workmen, the appropriate Government may, if it so thinks fit, make the reference to a Labour Court under clause (c):



Provided further that where the dispute relates to a public utility service and a notice under section 22 has been given, the appropriate Government shall, unless it considers that the notice has been frivolously or vexatiously given or that it would be inexpedient so to do, make a reference under this sub-section notwithstanding that any other proceedings under this Act in respect of the dispute may have commenced: Provided also that where the dispute in the relation to which the Central Government is the appropriate Government, it shall be competent for the Government to refer the dispute to a Labour Court or an Industrial Tribunal, as the case may be, constituted by the State Government.

- (1A) Where the Central Government is of opinion that any industrial dispute exists or is apprehended and the dispute involves any question of national importance or is of such a nature that industrial establishments situated in more than one State are likely to be interested in, or affected by, such dispute and that the dispute should be adjudicated by a National Tribunal, then, the Central Government may, whether or not it is the appropriate Government in relation to that dispute, at any time, by order in writing, refer the dispute or any matter appearing to be connected with, or relevant to, the dispute, whether it relates to any matter specified in the Second Schedule or the Third Schedule, to a National Tribunal for adjudication.
- (2) Where the parties to an industrial dispute apply in the prescribed manner, whether jointly or separately, for a reference of the dispute to a Board, Court, Labour Court, Tribunal or National Tribunal, the appropriate Government, if satisfied that the persons applying represent the majority of each party, shall make the reference accordingly.
- (2A) An order referring an industrial dispute to a Labour Court, Tribunal or National Tribunal under this section shall specify the period within which such Labour Court, Tribunal or National Tribunal shall submit its award on such dispute to the appropriate Government:

Provided that where such industrial dispute is connected with an individual workman, no such period shall exceed three months:

Provided further that where the parties to an industrial dispute apply in the person entitled, be recovered by that Government in the same manner as an arrear of land revenue.

- (8) Every Labour Court, Tribunal or National Tribunal shall be deemed to be Civil Court for the purposes of sections 345, 346 and 348 of the Code of Criminal Procedure, 1973 (2 of 1974).

VOLUNTARY REFERENCE OF DISPUTES TO (Sec 10A)

ARBITRATION

- (1) Where any industrial dispute exists or is apprehended and the employer and the workmen agree to refer the dispute to arbitration, they may, at any time before the dispute has been referred under section 10 to a Labour Court or Tribunal or National Tribunal, by a written agreement, refer the dispute to arbitration and the reference shall be to such person or persons (including the presiding officer of a Labour Court or Tribunal or National Tribunal) as an arbitrator or arbitrators as may be specified in the arbitration agreement.
- (1A) Where an arbitration agreement provides for a reference of the dispute to an even number of arbitrators, the agreement shall provide for the appointment of another person as umpire who shall enter upon the reference, if the arbitrators are equally divided in their opinion, and the award of the umpire shall prevail and shall be deemed to be the arbitration award for the purpose of this Act.
- (2) An arbitration agreement referred to in sub-section (1) shall be in such form and shall be signed by the parties thereto in such manner as may be prescribed.
- (3) A copy of the arbitration agreement shall be forwarded to the appropriate Government and the conciliation officer and the appropriate Government shall, within one month from the date of the receipt of such copy, publish the same in the Official Gazette.
- (3A) Where an industrial dispute has been referred to arbitration and the appropriate Government is satisfied that the persons making the reference represent the majority of each party, the appropriate Government may, within the time referred to in sub-section (3), issue a notification in such manner as may be prescribed; and when any such notification is issued, the employers and workmen who are



not parties to the arbitration agreement but are concerned in the dispute, shall be given an opportunity of presenting their case before the arbitrator or arbitrators.

- (4) The arbitrator or arbitrators shall investigate the dispute and submit to the appropriate Government the arbitration award signed by the arbitrator or all the arbitrators, as the case may be.
- (4A) Where an industrial dispute has been referred to arbitration and a notification has been issued under sub-section (3A), the appropriate Government may, by order, prohibit the continuance of any strike or lock-out in connection with such dispute which may be in existence on the date of the reference.
- (5) Nothing in the Arbitration Act, 1940 (10 of 1940) shall apply to arbitrations under this section.

PROCEDURE, POWERS AND DUTIES OF AUTHORITIES (Sec 11 to 21)

PROCEDURE AND POWER OF CONCILIATION OFFICERS, BOARDS, COURTS AND TRIBUNALS (Sec 11)

- (1) Subject to any rules that may be made in this behalf, an arbitrator, a Board, Court, Labour Court, Tribunal or National Tribunal shall follow such procedure as the arbitrator or other authority concerned may think fit.
- (2) A conciliation officer or a member of a Board, or court or the presiding officer of a Labour Court, Tribunal or National Tribunal may for the purpose of inquiry into any existing or apprehended industrial dispute, after giving reasonable notice, enter the premises occupied by any establishment to which the dispute relates.
- (3) Every Board, Court, Labour Court, Tribunal and National Tribunal shall have the same powers as are vested in a Civil Court under the Code of Civil Procedure, 1908 (5 of 1908), when trying a suit, in respect of the following matters, namely :
 - (a) enforcing the attendance of any person and examining him on oath;
 - (b) compelling the production of documents and material objects;
 - (c) issuing commissions for the examination of witnesses;
 - (d) in respect of such other matters as may be prescribed, and every inquiry or investigation by a Board, Court, Labour Court, Tribunal or National Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860).
- (4) A conciliation officer may enforce the attendance of any person for the purpose of examination of such person or call for and inspect any document which he has ground for considering to be relevant to the industrial dispute or to be necessary for the purpose of verifying the implementation of any award or carrying out any other duty imposed on him under this Act, and for the aforesaid purposes, the conciliation officer shall have the same powers as are vested in a Civil Court under the Code of Civil Procedure, 1908 (5 of 1908), in respect of enforcing the attendance of any person and examining him or of compelling the production of documents.
- (5) A Court, Labour Court, Tribunal or National Tribunal may, if it so thinks fit, appoint one or more persons having special knowledge of the matter under consideration as an assessor or assessors to advise it in the proceeding before it.
- (6) All conciliation officers, members of a Board or Court and the presiding officers of a Labour Court, Tribunal or National Tribunal shall be deemed to be public servants within the meaning of section 21 of the Indian Penal Code (45 of 1860).
- (7) Subject to any rules made under this Act, the costs of, and incidental to, any proceeding before a Labour Court, Tribunal or National Tribunal shall be in the discretion of that Labour Court, Tribunal or National Tribunal and the Labour Court, Tribunal or National Tribunal, as the case may be, shall have full power to determine by and to whom and to what extent and subject to what conditions, if any, such costs are to be paid, and to give all necessary directions for the purposes aforesaid and such costs may, on application made to the appropriate Government by the person entitled, be recovered by that Government in the same manner as an arrear of land revenue.
- (8) Every Labour Court, Tribunal or National Tribunal shall be deemed to be Civil Court for the purposes of sections 345, 346 and 348 of the Code of Criminal Procedure, 1973 (2 of 1974).



POWERS OF LABOUR COURTS, TRIBUNALS AND NATIONAL TRIBUNALS TO GIVE APPROPRIATE RELIEF IN CASE OF DISCHARGE OR DISMISSAL OF WORKMEN (Sec 11A)

Where an industrial dispute relating to the discharge or dismissal of a workman has been referred to a Labour Court, Tribunal or National Tribunal for adjudication and, in the course of the adjudication proceedings, the Labour Court, Tribunal or National Tribunal, as the case may be, is satisfied that the order of discharge or dismissal was not justified, it may, by its award, set aside the order of discharge or dismissal and direct re-instatement of the workman on such terms and conditions, if any, as it thinks fit, or give such other relief to the workman including the award of any lesser punishment in lieu of discharge or dismissal as the circumstances of the case may require:

Provided that in any proceeding under this section the Labour Court, Tribunal or National Tribunal, as the case may be, shall rely only on the materials on record and shall not take any fresh evidence in relation to the matter.

COMMENTS

- (i) The power under section 11A is akin to appellate power. The competent adjudicating Authority has jurisdiction to interfere with the quantum of punishment even in cases where finding of guilt recorded by the employer is upheld or in the case of no enquiry or defective enquiry; *Vidya Dhar v. The Hindustan Copper Ltd.*, 1994 LLR 229 (Raj).
- (ii) Once the misconduct is established, the maximum punishment stipulated therefor can be awarded. However, the Labour Court has full discretion to award lesser punishment; *Hindalco Workers Union v. Labour Court*, 1994 LLR 379 (All).
- (iii) The order of termination of services of a workman operates prospectively from the date on which it was passed; *Kumaon Motor Owner's Union Ltd. v. State of U.P.*, 1994 LLR 366 (All.).
- (iv) Labour Court has powers under section 11A of the Act to evaluate the gravity of the misconduct for the imposition of punishment on workman (who was found sleeping while on duty) and exercise its discretion; *Management, Lakshmi Machine Works Ltd. v. P.O. Labour Court, Coimbatore*, 1948 LLR 368.

DUTIES OF CONCILIATION OFFICERS (Sec 12)

- (1) Where any industrial dispute exists or is apprehended, the conciliation officer may, or where the dispute relates to a public utility service and a notice under section 22 has been given, shall, hold conciliation proceedings in the prescribed manner.
- (2) The conciliation officer shall, for the purpose of bringing about a settlement of the dispute without delay, investigate the dispute and all matters affecting the merits and right settlement thereof and may do all such things as he thinks fit, for the purpose of inducing the parties to come to a fair and amicable settlement of the dispute.
- (3) If a settlement of the dispute or of any of the matters in dispute is arrived at in the course of the conciliation proceedings, the conciliation officer shall send a report thereof to the appropriate Government or an officer authorised in this behalf, by the appropriate Government together with a memorandum of the settlement signed by the parties to the dispute.
- (4) If no such settlement is arrived at, the conciliation officer shall, as soon as practicable after the close of the investigation, send to the appropriate Government a full report setting forth the steps taken by him for ascertaining the facts and circumstances relating to the dispute and for bringing about a settlement thereof, together with a full statement of such facts and circumstances, and the reasons on account of which, in his opinion, a settlement could not be arrived at.
- (5) If, on a consideration of the report referred to in sub-section (4), the appropriate Government is satisfied that there is a case for reference to a Board, Labour Court, Tribunal or National Tribunal, it may make such reference. Where the appropriate Government does not make such a reference it shall record and communicate to the parties concerned its reasons therefor.
- (6) A report under this section shall be submitted within fourteen days of the commencement of the conciliation proceedings or within such shorter period as may be fixed by the appropriate Government: Provided that, subject to the approval of the conciliation officer, the time for the submission of the report may be extended by such period as may be agreed upon in writing by all the parties to the dispute.

**COMMENTS**

- (i) The appropriate Government acting under section 10 or section 12(5) of the Act has no power to decide the merits of the controversy. It can only determine whether dispute exists or not; *Sukhbir Singh v. Union of India*, 1994 LLR 375 (Del).
- (ii) According to section 12(5) of the Act, the appropriate Government, while rejecting the request for reference of the dispute to the Industrial Tribunal, is obliged to give reasons; *Sukhbir Singh v. Union of India*, 1994 LLR 375 (Del).

DUTIES OF BOARD (Sec 13)

- (1) Where a dispute has been referred to a Board under this Act, it shall be the duty of the Board to endeavour to bring about a settlement of the same and for this purpose the Board shall, in such manner as it thinks fit and without delay, investigate the dispute and all matters affecting the merits and the right settlement thereof and may do all such things as it thinks fit for the purpose of inducing the parties to come to a fair and amicable settlement of the dispute.
- (2) If a settlement of the dispute or of any of the matters in dispute is arrived at in the course of the conciliation proceedings, the Board shall send a report thereof to the appropriate Government together with a memorandum of the settlement signed by the parties to the dispute.
- (3) If no such settlement is arrived at, the Board shall, as soon as practicable after the close of the investigation, send to the appropriate Government a full report setting for the proceedings and steps taken by the Board for ascertaining the facts and circumstances relating to the dispute and for bringing about a settlement thereof, together with a full statement of such facts and circumstances, its findings thereon, the reasons on account of which, in its opinion, a settlement could not be arrived at and its recommendations for the determination of the dispute.
- (4) If, on the receipt of a report under sub-section (3) in respect of a dispute relating to a public utility service, the appropriate Government does not make a reference to a Labour Court, Tribunal or National Tribunal under section 10, it shall record and communicate to the parties concerned its reasons therefor.
- (5) The Board shall submit its report under this section within two months of the date on which the dispute was referred to it or within such shorter period as may be fixed by the appropriate Government:
Provided that the appropriate Government may from time to time extend the time for the submission of the report by such further periods not exceeding two months in the aggregate:
Provided further that the time for the submission of the report may be extended by such period as may be agreed on in writing by all the parties to the dispute.

DUTIES OF COURTS (Sec 14)

A Court shall inquire into the matters referred to it and report thereon to the appropriate Government ordinarily within a period of six months from the commencement of its inquiry.

DUTIES OF LABOUR COURTS, TRIBUNALS AND NATIONAL TRIBUNALS (Sec 15)

Where an industrial dispute has been referred to a Labour Court, Tribunal or National Tribunal for adjudication, it shall hold its proceedings expeditiously and shall, within the period specified in the order referring such industrial dispute or the further period extended under the second proviso to sub-section (2A) of section 10, submit its award to the appropriate Government.

FORM OF REPORT OR AWARD (Sec 16)

- (1) The report of a Board or Court shall be in writing and shall be signed by all the members of the Board or Court, as the case may be :
Provided that nothing in this section shall be deemed to prevent any member of the Board or Court from recording any minute of dissent from a report or from any recommendation made therein.
- (2) The award of a Labour Court or Tribunal or National Tribunal shall be in writing and shall be signed by its presiding officer.



PUBLICATION OF REPORTS AND AWARDS (Sec 17)

- (1) Every report of a Board or Court together with any minute of dissent recorded therewith, every arbitration award and every award of a Labour Court, Tribunal or National Tribunal shall, within a period of thirty days from the date of its receipt by the appropriate Government, be published in such manner as the appropriate Government thinks fit.
- (2) Subject to the provisions of section 17A, the award published under sub-section (1) shall be final and shall not be called in question by any court in any manner whatsoever.

COMMENCEMENT OF THE AWARD (Sec 17A)

- (1) An award (including an arbitration award) shall become enforceable on the expiry of thirty days from the date of its publication under section 17:
Provided that
 - (a) if the appropriate Government is of opinion, in any case where the award has been given by a Labour Court or Tribunal in relation to an industrial dispute to which it is a party; or
 - (b) if the Central Government is of opinion, in any case where the award has been given by a National Tribunal, that it will be inexpedient on public grounds affecting national economy or social justice to give effect to the whole or any part of the award, the appropriate Government, or as the case may be, the Central Government may, by notification in the Official Gazette, declare that the award shall not become enforceable on the expiry of the said period of thirty days.
- (2) Where any declaration has been made in relation to an award under the proviso to sub-section (1), the appropriate Government or the Central Government may, within ninety days from the date of publication of the award under section 17, make an order rejecting or modifying the award, and shall, on the first available opportunity, lay the award together with a copy of the order before the Legislature of the State, if the order has been made by a State Government, or before Parliament, if the order has been made by the Central Government.
- (3) Where any award as rejected or modified by an order made under sub-section (2) is laid before the Legislature of a State or before Parliament, such award shall become enforceable on the expiry of fifteen days from the date on which it is so laid; and where no order under sub-section (2) is made in pursuance of a declaration under the proviso to sub-section (1), the award shall become enforceable on the expiry of the period of ninety days referred to in sub-section (2).
- (4) Subject to the provisions of sub-section (1) and sub-section (3) regarding the enforceability of an award, the award shall come into operation with effect from such date as may be specified therein, but where no date is so specified, it shall come into operation on the date when the award becomes enforceable under sub-section (1) or sub-section (3), as the case may be.

COMMENTS

Held, Industrial Tribunal retains its jurisdiction to deal with an application for setting aside an *ex parte* award only until the expiry of 30 days from publication of the award. Thereafter, tribunal is relegated to the position of *functus officio*; *Ranigunj Chemical Works v. Learned Judge, Fourth Industrial Tribunal*, 1998 LLR 475

PAYMENT OF FULL WAGES TO WORKMAN PENDING PROCEEDINGS IN HIGHER COURTS (Sec 17B)

Where in any case, a Labour Court, Tribunal or National Tribunal by its award directs reinstatement of any workman and the employer prefers any proceedings against such award in a High Court or the Supreme Court, the employer shall be liable to pay such workman, during the period of pendency of such proceedings in the High Court or the Supreme Court, full wages last drawn by him, inclusive of any maintenance allowance admissible to him under any rule if the workman had not been employed in any establishment during such period and an affidavit by such workman had been filed to that effect in such court:

Provided that where it is proved to the satisfaction of the High Court or the Supreme Court that such workman had been employed and had been receiving adequate remuneration during any such period or part thereof, the court shall order that no wages shall be payable under this section for such period or part, as the case may be.

- (i) it is commenced or declared in contravention of section 22 or section 23; or



- (ii) it is continued in contravention of an order made under sub-section (3) of section 10 or sub-section (4A) of section 10A.
- (2) Where a strike or lock-out in pursuance of an industrial dispute has already commenced and is in existence at the time of the reference of the dispute to a Board, an arbitrator, a Labour Court, Tribunal or National Tribunal, the continuance of such strike or lock-out shall not be deemed to be illegal, provided that such strike or lock-out was not at its commencement in contravention of the provisions of this Act or the continuance thereof was not prohibited under sub-section (3) of section 10 or sub-section (4A) of section 10A
- (3) A lock-out declared in consequence of an illegal strike or a strike declared in consequence of an illegal lock-out shall not be deemed to be illegal.

PERSONS ON WHOM SETTLEMENTS AND AWARDS ARE BINDING (Sec 18)

- (1) A settlement arrived at by agreement between the employer and workman otherwise than in the course of conciliation proceeding shall be binding on the parties to the agreement.
- (2) Subject to the provisions of sub-section (3), an arbitration award which has become enforceable shall be binding on the parties to the agreement who referred the dispute to arbitration.
- (3) A settlement arrived at in the course of conciliation proceedings under this Act or an arbitration award in a case where a notification has been issued under sub-section (3A) of section 10A or an award of a Labour Court, Tribunal or National Tribunal which has become enforceable shall be binding on:
 - (a) all parties to the industrial dispute;
 - (b) all other parties summoned to appear in the proceedings as parties to the dispute, unless the Board, arbitrator Labour Court, Tribunal or National Tribunal, as the case may be, records the opinion that they were so summoned without proper cause;
 - (c) where a party referred to in clause (a) or clause (b) is an employer, his heirs, successors or assigns in respect of the establishment to which the dispute relates;
 - (d) where a party referred to in clause (a) or clause (b) is composed of workmen, all persons who were employed in the establishment or part of the establishment, as the case may be, to which the dispute relates on the date of the dispute and all persons who subsequently become employed in that establishment or part.

COMMENTS

Settlements are divided into two categories, namely. (i) those arrived at outside the conciliation proceedings; and (ii) those arrived at in the course of conciliation proceedings. A settlement arrived at in the course of conciliation proceedings with a recognised majority union will be binding on all workmen of the establishment irrespective of any objection; *All India Textile Janta Union v. The Labour Commissioner*, 1994 LLR 203 (P&H) (DB).

PERIOD OF OPERATION OF SETTLEMENTS AND AWARDS (Sec 19)

- (1) A settlement shall come into operation on such date as is agreed upon by the parties to the dispute, and if no date is agreed upon, on the date on which the memorandum of the settlement is signed by the parties to the dispute.
- (2) Such settlement shall be binding for such period as is agreed upon by the parties, and if no such period is agreed upon, for a period of six months from the date on which the memorandum of settlement is signed by the parties to the dispute, and shall continue to be binding on the parties after the expiry of the period aforesaid, until the expiry of two months from the date on which a notice in writing of an intention to terminate the settlement is given by one of the parties to the other party or parties to the settlement.
- (3) An award shall, subject to the provisions of this section, remain in operation for a period of one year from the date on which the award becomes enforceable under section 17A:

Provided that the appropriate Government may reduce the said period and fix such period as it thinks fit:

Provided further that the appropriate Government may, before the expiry of the said period, extend the period of operation by any period not exceeding one year at a time as it thinks fit so, however,



that the total period of operation of any award does not exceed three years from the date on which it came into operation.

- (4) Where the appropriate Government, whether of its own motion or on the application of any party bound by the award, considers that since the award was made, there has been a material change in the circumstances on which it was based, the appropriate Government may refer the award or a part of it to a Labour Court, if the award was that of a Labour Court or to a Tribunal, if the award was that of a Tribunal or of a National Tribunal, for decision whether the period of operation should not, by reason of such change, be shortened and the decision of Labour Court or the Tribunal, as the case may be on such reference shall, be final.
- (5) Nothing contained in sub-section (3) shall apply to any award which by its nature, terms or other circumstances does not impose, after it has been given effect to, any continuing obligation on the parties bound by the award.
- (6) Notwithstanding the expiry of the period of operation under sub-section (3), the award shall continue to be binding on the parties until a period of two months has elapsed from the date on which notice is given by any party bound by the award to the other party or parties intimating its intention to terminate the award.
- (7) No notice given under sub-section (2) or sub-section (6) shall have effect, unless it is given by a party representing the majority of persons bound by the settlement or award, as the case may be.

COMMENCEMENT AND CONCLUSION OF PROCEEDINGS (Sec 20)

- (1) A conciliation proceeding shall be deemed to have commenced on the date on which a notice of strike or lock-out under section 22 is received by the conciliation officer or on the date of the order referring the dispute to a Board, as the case may be.
- (2) A conciliation proceeding shall be deemed to have concluded :
 - (a) where a settlement is arrived at, when a memorandum of the settlement is signed by the parties to the dispute;
 - (b) where no settlement is arrived at, when the report of the conciliation officer is received by the appropriate Government or when the report of the Board is published under section 17, as the case may be; or
 - (c) when a reference is made to a court, Labour Court, Tribunal or National Tribunal under section 10 during the pendency of conciliation proceedings.
- (3) Proceedings before an arbitrator under section 10A or before a Labour Court, Tribunal or National Tribunal shall be deemed to have commenced on the date of the reference of the dispute for arbitration or adjudication, as the case may be and such proceedings shall be deemed to have concluded on the date on which the award becomes enforceable under section 17A.

CERTAIN MATTERS TO BE KEPT CONFIDENTIAL (Sec 21)

There shall not be included in any report or award under this Act, any information obtained by a conciliation officer, Board, Court, Labour Court, Tribunal, National Tribunal or an arbitrator in the course of any investigation or inquiry as to a trade union or as to any individual business (whether carried on by a person, firm or company) which is not available otherwise than through the evidence given before such officer, Board, Court, Labour Court, Tribunal, National Tribunal or arbitrator, if the trade union, person, firm or company, in question has made a request in writing to the conciliation officer, Board, Court Labour Court, Tribunal, National Tribunal or arbitrator, as the case may be, that such information shall be treated as confidential; nor shall such conciliation officer or any individual member of the Board, or Court or the presiding officer of the Labour Court, Tribunal or National Tribunal or the arbitrator or any person present at or concerned in the proceedings disclose any such information without the consent in writing of the secretary of the trade union or the person, firm or company in question, as the case may be:

Provided that nothing contained in this section shall apply to a disclosure of any such information for the purposes of a prosecution under section 193 of the Indian Penal Code (45 of 1860).

**STRIKES AND LOCK-OUTS****PROHIBITION OF STRIKES AND LOCK-OUTS (Sec 22)**

- (1) No person employed in a public utility service shall go on strike, in breach of contract:
 - (a) without giving to the employer notice of strike, as hereinafter provided, within six weeks before striking; or
 - (b) within fourteen days of giving such notice; or
 - (c) before the expiry of the date of strike specified in any such notice as aforesaid; or
 - (d) during the pendency of any conciliation proceedings before a conciliation officer and seven days after the conclusion of such proceedings.
- (2) No employer carrying on any public utility service shall lock-out any of his workman:
 - (a) without giving them notice of lock-out as hereinafter provided, within six weeks before locking-out; or
 - (b) within fourteen days of giving such notice; or
 - (c) before the expiry of the date of lock-out specified in any such notice as aforesaid; or
 - (d) during the pendency of any conciliation proceedings before a conciliation officer and seven days after the conclusion of such proceedings.
- (3) The notice of lock-out or strike under this section shall not be necessary where there is already in existence a strike or, as the case may be, lock-out in the public utility service, but the employer shall send intimation of such lock-out or strike on the day on which it is declared, to such Authority as may be specified by the appropriate Government either generally or for a particular area or for a particular class of public utility services.
- (4) The notice of strike referred to in sub-section (1) shall be given by such number of persons to such person or persons and in such manner as may be prescribed.
- (5) The notice of lock-out referred to in sub-section (2) shall be given in such manner as may be prescribed.
- (6) If on any day an employer receives from any person employed by him any such notices as are referred to in sub-section (1) or gives to any persons employed by him any such notices as are referred to in sub-section (2), he shall within five days, thereof report to the appropriate Government or to such authority as that Government may prescribe the number of such notices received or given on that day.

GENERAL PROHIBITION OF STRIKES AND LOCK-OUTS (Sec 23)

No workman who is employed in any industrial establishment shall go on strike in breach of contract and no employer of any such workman shall declare a lock-out

- (a) during the pendency of conciliation proceedings before a Board and seven days after the conclusion of such proceedings;
- (b) during the pendency of proceedings before a Labour Court, Tribunal or National Tribunal and two months, after the conclusion of such proceedings;
- (bb) during the pendency of arbitration proceedings before an arbitrator and two months after the conclusion of such proceedings, where a notification has been issued under sub-section (3A) of section 10A; or
- (c) during any period in which a settlement or award is in operation, in respect of any of the matters covered by the settlement or award.

ILLEGAL STRIKES AND LOCK-OUTS (Sec 24)

- (1) A strike or a lock-out shall be illegal if—
 - (i) it is commenced or declared in contravention of section 22 or section 23; or
 - (ii) it is continued in contravention of an order made under sub-section (3) of section 10 or sub-section (4A) of section 10A.



- (2) Where a strike or lock-out in pursuance of an industrial dispute has already commenced and is in existence at the time of the reference of the dispute to a Board, an arbitrator, a Labour Court, Tribunal or National Tribunal, the continuance of such strike or lock-out shall not be deemed to be illegal, provided that such strike or lock-out was not at its commencement in contravention of the provisions of this Act or the continuance thereof was not prohibited under sub-section (3) of section 10 or sub-section (4A) of section 10A.
- (3) A lock-out declared in consequence of an illegal strike or a strike declared in consequence of an illegal lock-out shall not be deemed to be illegal.

COMMENTS

This section deals with the permission for closure of undertaking; *Union Carbide Karamchari Sangh v. Union of India*, 1993 LLR 481 (MP).

PROHIBITION OF FINANCIAL AID TO ILLEGAL STRIKES AND LOCK-OUTS (Sec 25)

No person shall knowingly expend or apply any money in direct furtherance or support of any illegal strike or lock-out.

LAY-OFF AND RETRENCHMENT

APPLICATION OF SECTIONS 25C TO 25E (Sec 25A)

- (1) Sections 25C to 25E inclusive shall not apply to Industrial Establishments to which Chapter VB applies, or
 - (a) to industrial establishments in which less than fifty workmen on an average per working day have been employed in the preceding calendar month; or
 - (b) to industrial establishments which are of a seasonal character or in which work is performed only intermittently.
- (2) If a question arises whether an industrial establishment is of a seasonal character or whether work is performed therein only intermittently, the decision of the appropriate Government thereon shall be final.

Explanation- In this section and in sections 25C, 25D and 25E, "industrial establishment" means—

- (i) a factory as defined in clause (m) of section 2 of the Factories Act, 1948 (63 of 1948); or
- (ii) a mine as defined in clause (j) of section 2 of the Mines Act, 1952 (35 of 1952); or
- (iii) a plantation as defined in clause (f) of section 2 of the Plantations Labour Act, 1951 (69 of 1951).

DEFINITION OF CONTINUOUS SERVICE (Sec 25B)

For the purposes of this Chapter:

- (1) a workman shall be said to be in continuous service for a period if he is, for that period, in uninterrupted service, including service which may be interrupted on account of sickness or authorised leave or an accident or as strike which is not illegal, or a lock-out or a cessation of work which is not due to any fault on the part of the workman;
- (2) where a workman is not in continuous service within the meaning of clause (1) for a period of one year or six months, he shall be deemed to be in continuous service under an employer:
 - (a) for a period of one year, if the workman, during a period of twelve calendar months preceding the date with reference to which calculation is to be made, has actually worked under the employer for not less than
 - (i) one hundred and ninety days in the case of a workman employed below ground in a mine; and
 - (ii) two hundred and forty days, in any other case;
 - (b) for a period of six months, if the workman, during a period of six calendar months preceding the date with reference to which calculation is to be made, has actually worked under the employer for not less than



- (i) ninety-five days, in the case of workman employed below ground in a mine; and
- (ii) one hundred and twenty days, in any other case.

Explanation : For the purposes of clause (2), the number of days on which a workman has actually worked under an employer shall include the days on which:

- (i) he has been laid-off under an agreement or as permitted by standing orders made under the Industrial Employment (Standing Orders) Act, 1946 (20 of 1946), or under the Act or under any other law applicable to the industrial establishment;
- (ii) he has been on leave with full wages, earned in the previous years;
- (iii) he has been absent due to temporary disablement caused by accident arising out of and in the course of his employment; and
- (iv) in the case of a female, she has been on maternity leave; so, however, that the total period of such maternity leave does not exceed twelve weeks.

COMMENTS

- (i) A workman is deemed to be in continuous service for a period of one year, if he, during the period of twelve calendar months preceding the date of termination, has actually worked under the employer for not less than 240 days; *Gram Panchayat v. Sharadkumar D. Acharya*, 1994 LLR 470 (Guj) (DB).
- (ii) Only cases not falling under sub-section (1) are covered by sub-section (2) of section 25B; *G. Yadi Reddy v. Brook Bond India Ltd.*, 1994 LLR 328 (AP) (DB).
- (iii) In the computation of the period under sub-section (2) of section 25B, Sundays and holidays should be taken into account; *G. Yadi Reddy v. Brook Bond India Ltd.*, 1994 LLR 328 (AP) (DB).

RIGHT OF WORKMEN LAID-OFF FOR COMPENSATION (Sec 25C)

Whenever a workman (other than a *badli* workman or a casual workman) whose name is borne on the muster rolls of an industrial establishment and who has completed not less than one year of continuous service under an employer is laid-off, whether continuously or intermittently, he shall be paid by the employer for all days during which he is so laid-off, except for such weekly holidays as may intervene, compensation which shall be equal to fifty per cent, of the total of the basic wages and dearness allowance that would have been payable to him had he not been so laid-off:

Provided that if during any period of twelve months, a workman is so laid-off for more than forty-five days, no such compensation shall be payable in respect of any period of the lay-off after the expiry of the first forty-five days, if there is an agreement to that effect between the workman and the employer:

Provided further that it shall be lawful for the employer in any case falling within the foregoing proviso to retrench the workman in accordance with the provisions contained in section 25F at any time after the expiry of the first forty-five days of the lay-off and when he does so, any compensation paid to the workman for having been laid-off during the preceding twelve months may be set off against the compensation payable for retrenchment.

Explanation : “*Badli workman*” means a workman who is employed in an industrial establishment in the place of another workman whose name is borne on the muster rolls of the establishment, but shall cease to be regarded as such for the purposes of this section, if he has completed one year of continuous service in the establishment.

DUTY OF AN EMPLOYER TO MAINTAIN MUSTER ROLLS OF WORK (Sec 25D)

MEN—Notwithstanding that workmen in any industrial establishment have been laid-off, it shall be the duty of every employer to maintain for the purposes of this Chapter a muster roll, and to provide for the making of entries therein by workmen who may present themselves for work at the establishment at the appointed time during normal working hours.

WORKMEN NOT ENTITLED TO COMPENSATION IN CERTAIN CASES (Sec 25E)

No compensation shall be paid to a workman who has been laid-off :

- (i) if he refuses to accept any alternative employment in the same establishment from which he has been laid-off, or in any other establishment belonging to the same employer situate in the same



town or village or situate within a radius of five miles from the establishment to which he belongs, if, in the opinion of the employer, such alternative employment does not call for any special skill or previous experience and can be done by the workman, provided that the wages which would normally have been paid to the workman are offered for the alternative employment also;

- (ii) if he does not present himself for work at the establishment at the appointed time during normal working hours at least once a day;
- (iii) if such laying-off is due to a strike or slowing-down of production on the part of workmen in another part of the establishment.

CONDITIONS PRECEDENT TO RETRENCHMENT OF WORKMEN (Sec 25F)

No workman employed in any industry who has been in continuous service for not less than one year under an employer shall be retrenched by that employer until—

- (a) the workman has been given one month's notice in writing indicating the reasons for retrenchment and the period of notice has expired, or the workman has been paid in lieu of such notice, wages for the period of the notice;
- (b) the workman has been paid, at the time of retrenchment, compensation which shall be equivalent to fifteen days' average pay for every completed year of continuous service or any part thereof in excess of six months; and
- (c) notice in the prescribed manner is served on the appropriate Government for such Authority, as may be specified by the appropriate Government, by notification in the Official Gazette.

COMMENTS

- (i) Termination does not amount to retrenchment and therefore provision of section 25F is not attracted; *Life Insurance Corporation of India v. Rajeev Kumar Srivastava*, 1994 LLR 573 (All) (DB).
- (ii) The conditions enumerated in section 25F are condition precedent; *State of Rajasthan v. Miss Usha Lokwani*, 1994 LLR 369 (Raj).
- (iii) The provisions of section 25F are couched in mandatory form, and non-compliance therewith has the result of rendering the order of retrenchment void *ab initio* or *non-est*; *State of Rajasthan v. Miss Usha Lokwani*, 1994 LLR 369 (Raj).
- (iv) It is well established that the period of cessation of work not due to any fault on the part of the employee, always gets calculated as a period of continuous service; *Kukadi Irrigation Project v. Waman*, 1994 LLR 381 (Bom).

COMPENSATION TO WORKMEN IN CASE OF TRANSFER OF UNDERTAKINGS (Sec 25FF)

Where the ownership of management of an undertaking is transferred, whether by agreement or by operation of law, from the employer in relation to or that undertaking to a new employer, every workman who has been in continuous service for not less than one year in that undertaking immediately before such transfer shall be entitled to notice and compensation in accordance with the provisions of section 25F, as if the workman had been retrenched :

Provided that nothing in this section shall apply to a workman in any case where there has been a change of employers by reason of the transfer, if—

- (a) The service of the workman has not been interrupted by such transfer;
- (b) The terms and conditions of service applicable to the workman after such transfer are not in any way less favourable to the workman than those applicable to him immediately before the transfer; and section 2,
 - (i) In relation to any company in which not less than fifty-one per cent. of the paid-up share capital is held by the Central Government, or
 - (ii) In relation to any corporation not being a corporation referred to in sub-clause (i) of clause (a) of section 2 established by or under any law made by Parliament, the Central Government shall be the appropriate Government.

**PROHIBITION OF LAY-OFF (Sec 25M)**

- (1) No workman (other than a *badli* workman or a casual workman) whose name is borne on the muster rolls of an industrial establishment to which this Chapter applies shall be laid-off by his employer except with the prior permission of the appropriate Government or such authority as may be specified by that Government by notification in the Official Gazette (hereafter in this section referred to as the specified authority), obtained on an application made in this behalf, unless such lay-off is due to shortage of power or to natural calamity, and in the case of a mine, such lay-off is due also to fire, flood, excess of inflammable gas or explosion.
- (2) An application for permission under sub-section (1) shall be made by the employer in the prescribed manner stating clearly the reasons for the intended lay-off and a copy of such application shall also be served simultaneously on the workmen concerned in the prescribed manner.
- (3) Where the workmen (other than *badli* workmen or casual workmen) of an industrial establishment, being a mine, have been laid-off under sub-section (1) for reasons of fire, flood or excess of inflammable gas or explosion, the employer, in relation to such establishment, shall, within a period of thirty days from the date of commencement of such lay-off, apply, in the prescribed manner, to the appropriate Government or the specified authority for permission to continue the lay-off.
- (4) Where an application for permission under sub-section (1) or sub-section (3) has been made, the appropriate Government or the specified authority, after making such enquiry as it thinks fit and after giving a reasonable opportunity of being heard to the employer, the workmen concerned and the persons interested in such lay-off, may, having regard to the genuineness and adequacy of the reasons for such lay-off, the interests of the workmen and all other relevant factors, by order and for reasons to be recorded in writing, grant or refuse to grant such permission and a copy of such order shall be communicated to the employer and the workmen.
- (5) Where an application for permission under sub-section (1) or sub-section (3) has been made and the appropriate Government or the specified Authority does not communicate the order granting or refusing to grant permission to the employer within a period of sixty days from the date on which such application is made, the permission applied for shall be deemed to have been granted on the expiration of the said period of sixty days.
- (6) An order of the appropriate Government or the specified authority granting or refusing to grant permission shall, subject to the provisions of sub-section (7), be final and binding on all the parties concerned and shall remain in force for one year from the date of such order.
- (7) The appropriate Government or the specified authority may, either on its own motion or on the application made by the employer or any workman, review its order granting or refusing to grant permission under sub-section (4) or refer the matter or, as the case may be, cause it to be referred, to a Tribunal for adjudication :
Provided that where a reference has been made to a Tribunal under this sub-section, it shall pass an award within a period of thirty days from the date of such reference.
- (8) Where no application for permission under sub-section (1) is made, or where no application for permission under sub-section (3) is made within the period specified therein, or where the permission for any lay-off has been refused, such lay-off shall be deemed to be illegal from the date on which the workmen had been laid-off and the workmen shall be entitled to all the benefits under any law for the time being in force as if they had not been laid-off.
- (9) Notwithstanding anything contained in the foregoing provisions of this section, the appropriate Government may, if it is satisfied that owing to such exceptional circumstances as accident in the establishment or death of the employer or the like, it is necessary so to do, by order, direct that the provisions of sub-section (1), or, as the case may be, sub-section (3) shall not apply in relation to such establishment for such period as may be specified in the order.
- (10) The provisions of section 25C (other than the second proviso thereto) shall apply to cases of lay-off referred to in this section.

Explanation : For the purposes of this section, a workman shall not be deemed to be laid-off by an employer if such employer offers any alternative employment (which in the opinion of the employer does not call for any special skill or previous experience and can be done by the workman) in the same establishment



from which he has been laid-off or in any other establishment belonging to the same employer, situate in the same town or village, or situate within such distance from the establishment to which he belongs that the transfer will not involve undue hardship to the workman having regard to the facts and circumstances of his case, provided that the wages which would normally have been paid to the workman are offered for the alternative appointment also.

COMMENTS

In order to prevent hardship to the employees and to maintain higher tempo of production and productivity, section 25M of the Act puts some reasonable restrictions on the employer's right to lay-off, retrenchment and closure; *Central Pulp Mills Ltd. v. Central Pulp Mills Employees Union*, 1994 LLR. 130 (Guj) (DB).

CONDITIONS PRECEDENT TO RETRENCHMENT OF WORKMEN (Sec 25N)

- (1) No workman employed in any industrial establishment to which this Chapter applies, who has been in continuous service for not less than one year under an employer shall be retrenched by that employer until :
 - (a) The workman has been given three months' notice in writing indicating the reasons for retrenchment and the period of notice has expired, or the workman has been paid in lieu of such notice, wages for the period of the notice; and
 - (b) The prior permission of the appropriate Government or such authority as may be specified by that Government, by notification in the Official Gazette (hereafter in this section referred to as the specified authority), has been obtained on an application made in this behalf.
- (2) An application for permission under sub-section (1) shall be made by the employer in the prescribed manner stating clearly the reasons for the intended retrenchment and a copy of such application shall also be served simultaneously on the workmen concerned in the prescribed manner.
- (3) Where an application for permission under sub-section (1) has been made, the appropriate Government or the specified authority, after making such enquiry as it thinks fit and after giving a reasonable opportunity of being heard to the employer, the workmen concerned and the person interested in such retrenchment, may, having regard to the genuineness and adequacy of the reasons stated by the employer, the interests of the workmen and all other relevant factors, by order and for reasons to be recorded in writing, grant or refuse to grant such permission and a copy of such order shall be communicated to the employer and the workmen.
- (4) Where an application for permission has been made under sub-section (1) and the appropriate Government or the specified authority does not communicate the order granting or refusing to grant permission to the employer within a period of sixty days from the date on which such application is made, the permission applied for shall be deemed to have been granted on the expiration of the said period of sixty days.
- (5) An order of the appropriate Government or the specified Authority granting or refusing to grant permission shall, subject to the provisions of sub-section (6), be final and binding on all the parties concerned and shall remain in force for one year from the date of such order.
- (6) The appropriate Government or the specified Authority may, either on its own motion or on the application made by the employer or any workman, review its order granting or refusing to grant permission under sub-section (3) or refer the matter or, as the case may be, cause it to be referred, to a Tribunal for adjudication:

Provided that where a reference has been made to a Tribunal under this sub-section, it shall pass an award within a period of thirty days from the date of such reference.
- (7) Where no application for permission under sub-section (1) is made, or where the permission for any retrenchment has been refused, such retrenchment shall be deemed to be illegal from the date on which the notice of retrenchment was given to the workman and the workman shall be entitled to all the benefits under any law for the time being in force as if no notice had been given to him.
- (8) Notwithstanding anything contained in the foregoing provisions of this section, the appropriate Government may, if it is satisfied that owing to such exceptional circumstances as accident in the establishment or death of the employer or the like, it is necessary so to do, by order, direct that the



provisions of sub-section (1) shall not apply in relation to such establishment for such period as may be specified in the order.

- (9) Where permission for retrenchment has been granted under sub-section (3) or where permission for retrenchment is deemed to be granted under, sub-section (4), every workman who is employed in that establishment immediately before the date of application for permission under this section shall be entitled to receive, at the time of retrenchment, compensation which shall be equivalent to fifteen days' average pay for every completed year of continuous service or any part thereof in excess of six months.

COMMENTS

It is incumbent on the management to prove that the copies of the application as required by section 25N read with rule 76A of the Industrial Disputes Rules, 1957, were served on the concerned workman; *Shiv Kumar v. State of Haryana*, 1994 LLR 522 (SC).

PROCEDURE FOR CLOSING DOWN AN UNDERTAKING (Sec 25-O)

- (1) An employer who intends to close down an undertaking of an industrial establishment to which this Chapter applies shall, in the prescribed manner, apply, for prior permission at least ninety days before the date on which the intended closure is to become effective, to the appropriate Government, stating clearly the reasons for the intended closure of the undertaking and a copy of such application shall also be served simultaneously on the representatives of the workmen in the prescribed manner :
Provided that nothing in this sub-section shall apply to an undertaking set up for the construction of buildings, bridges, roads, canals, dams or for other construction work.
- (2) Where an application for permission has been made under sub-section (1) the appropriate Government, after making such enquiry as it thinks fit and after giving a reasonable opportunity of being heard to the employer, the workmen and the persons interested in such closure may, having regard to the genuineness and adequacy of the reasons stated by the employer, the interests of the general public and all other relevant factors, by order and for reasons to be recorded in writing, grant or refuse to grant such permission and a copy of such order shall be communicated to the employer and the workmen.
- (3) Where an application has been made under sub-section (1) and the appropriate Government does not communicate the order granting or refusing to grant permission to the employer within a period of sixty days from the date on which such application is made, the permission applied for shall be deemed to have been granted on the expiration of the said period of sixty days.
- (4) An order of the appropriate Government granting or refusing to grant permission shall, subject to the provisions of sub-section (5), be final and binding on all the parties and shall remain in force for one year from the date of such order.
- (5) The appropriate Government may, either on its own motion or on the application made by the employer or any workman, review its order granting or refusing to grant permission under sub-section (2) or refer the matter to a tribunal for adjudication : which the proceeding is pending for approval of the action taken by the employer.
- (6) Notwithstanding anything contained in sub-section (2), no employer shall, during the pendency of any such proceeding in respect of an industrial dispute, take any action against any protected workman concerned in such dispute
 - (a) by altering, to the prejudice of such protected workman, the conditions of service applicable to him immediately before the commencement of such proceeding; or
 - (b) by discharging or punishing, whether by dismissal or otherwise, such protected workman, save with the express permission in writing of the authority before which the proceeding is pending.

Explanation : For the purposes of this sub-section, a “**protected workman**”, in relation to an establishment, means a workman who, being a member of the executive or other office-bearer of a registered trade union connected with the establishment, is recognised as such in accordance with rules made in this behalf.

- (7) In every establishment, the number of workmen to be recognised as protected workmen for the purposes of sub-section (3) shall be one per cent of the total number of workmen employed therein



subject to a minimum number of five protected workmen and a maximum number of one hundred protected workmen and for the aforesaid purpose, the appropriate Government may make rules providing for the distribution of such protected workmen among various trade unions, if any, connected with the establishment and the manner in which the workmen may be chosen and recognised as protected workmen.

- (8) Where an employer makes an application to a conciliation officer, Board, an arbitrator, a Labour Court, Tribunal or National Tribunal under the proviso to sub-section (2) for approval of the action taken by him, the authority concerned shall, without delay, hear such application and pass, within a period of three months from the date of receipt of such application, such order in relation thereto as it deems fit:

Provided that where any such authority considers it necessary or expedient so to do, it may, for reasons to be recorded in writing, extend such period by such further period as it may think fit:

Provided further that no proceedings before any such authority shall lapse merely on the ground that any period specified in this sub-section had expired without such proceedings being completed.

COMMENTS

- (i) Violation of the provisions of section 33 of the Act entitles the workman to file a complaint under section 33A thereof and makes the employer liable to be punished. It, however, does not automatically entitle the employee to claim re-instatement; *Kimti Lal v. State of Haryana*, 1994 LLR 212 (P&H).
- (ii) Where there are more than one unions in operation, every union will have to be given the representation; *Maharashtra State Road Transport Corporation v. The Conciliation Officer*, 1994 LLR 196 (Bom).
- (iii) If approval is not granted the order of dismissal or discharge shall not be operative and the employee concerned shall be deemed to be in service; *G.K. Sengupta v. Hindustan Construction Co. Ltd.*, 1994 LLR 550 (Bom).
- (iv) Permission should be refused if the Tribunal is satisfied that the management's action is not *bona fide* or that the principles of natural justice have been violated or that the material on the basis of which the management came to a certain conclusion would not justify any reasonable person in coming to such a conclusion; *G.K. Sengupta v. Hindustan Construction Co. Ltd.*, 1994 LLR 550 (Bom).

SPECIAL PROVISION AS TO RESTARTING UNDERTAKINGS CLOSED DOWN BEFORE COMMENCEMENT OF THE INDUSTRIAL DISPUTES (AMENDMENT) ACT, 1976 (Sec 25P)

If the appropriate Government is of opinion in respect of any undertaking or an industrial establishment to which this Chapter applies and which closed down before the commencement of the Industrial Disputes (Amendment) Act, 1976 (32 of 1976):

- (a) That such undertaking was closed down otherwise than on account of unavoidable circumstances beyond the control of the employer;
- (b) That there are possibilities of restarting the undertaking;
- (c) That it is necessary for the rehabilitation of the workmen employed in such undertaking before its closure or for the maintenance of supplies and services essential to the life of the community to restart the undertaking or both; and
- (d) That the restarting of the undertaking will not result in hardship to the employer in relation to the undertaking, it may, after giving an opportunity to such employer and workmen, direct, by order published in the Official Gazette, that the undertaking shall be restarted within such time (not being less than one month from the date of the order) as may be specified in the order.

PENALTY FOR LAY-OFF AND RETRENCHMENT WITHOUT PREVIOUS PERMISSION (Sec 25Q)

Any employer who contravenes the provisions of section 25M or section 25N shall be punishable with imprisonment for a term which may extend to one month, or with fine which may extend to one thousand rupees, or with both.

PENALTY FOR CLOSURE (Sec 25R)

- (1) Any employer who closes down an undertaking without complying with the provisions of sub-section (1) of section 25-O shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to five thousand rupees, or with both.



- (2) Any employer, who contravenes an order refusing to grant permission to close down an undertaking under sub-section (2) of section 25-O or a direction given under section 25P, shall be punishable with imprisonment for a term which may extend to one year, or with fine which may extend to five thousand rupees, or with both, and where the contravention is a continuing one, with a further fine which may extend to two thousand rupees for every day during which the contravention continues after the conviction.

CERTAIN PROVISIONS OF CHAPTER VA TO APPLY TO INDUSTRIAL ESTABLISHMENT TO WHICH THIS CHAPTER APPLIES (Sec 25S)

The provisions of sections 25B, 25D, 25FF, 25G, 25H and 25J in Chapter VA shall, so far as may be, apply also in relation to an industrial establishment to which the provisions of this Chapter apply.

UNFAIR LABOUR PRACTICES

PROHIBITION OF UNFAIR LABOUR PRACTICE (Sec 25T)

No employer or workman or a trade union, whether registered under the Trade Unions Act, 1926 (16 of 1926), or not, shall commit any unfair labour practice.

PENALTY FOR COMMITTING UNFAIR LABOUR PRACTICES (Sec 25U)

Any person who commits any unfair labour practice shall be punishable with imprisonment for a term which may extend to six months or with fine which may extend to one thousand rupees or with both.

PENALTIES (Sec 26-31)

PENALTY FOR ILLEGAL STRIKES AND LOCK-OUTS (Sec 26)

- (1) Any workman who commences, continues or otherwise acts in furtherance of, a strike which is illegal under this Act, shall be punishable with imprisonment for a term which may extend to one month, or with fine which may extend to fifty rupees, or with both.
- (2) Any employer who commences, continues, or otherwise acts in furtherance of a lock-out which is illegal under this Act, shall be punishable with imprisonment for a term which may extend to one month, or with fine which may extend to one thousand rupees, or with both.

PENALTY FOR INSTIGATION, ETC (Sec 27)

Any person who instigates or incites others to take part in, or otherwise acts in furtherance of, a strike or lock-out which is illegal under this Act, shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both.

28. PENALTY FOR GIVING FINANCIAL AID TO ILLEGAL STRIKES AND LOCK-OUTS (Sec 28)

Any person who knowingly expends or applies any money in direct furtherance or support of any illegal strike or lock-out shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both.

PENALTY FOR BREACH OF SETTLEMENT OR AWARD (Sec 29)

Any person who commits a breach of any term of any settlement or award, which is binding on him under this Act, shall be punishable with imprisonment for a term which may extend to six months, or with fine, or with both, and where the breach is a continuing one, with a further fine which may extend to two hundred rupees for every day during which the breach continues after the conviction for the first and the court trying the offence, if it fines the offender, may direct that the whole or any part of the fine realised from him shall be paid, by way of compensation, to any person who, in its opinion has been injured by such breach.

PENALTY FOR DISCLOSING CONFIDENTIAL INFORMATION (Sec 30)

Any person who wilfully discloses any such information as is referred to in section 21 in contravention of the provisions of that section shall, on complaint made by or on behalf of the trade union or individual business affected, be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both.



PENALTY FOR CLOSURE WITHOUT NOTICE (Sec 30A)

Any employer who closes down any undertaking without complying with the provisions of section 25FFA shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to five thousand rupees, or with both.

PENALTY FOR OTHER OFFENCES (Sec 31)

- (1) Any employer who contravenes the provisions of section 33 shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both.
- (2) Whoever contravenes any of the provisions of this Act or any rule made thereunder shall, if no other penalty is elsewhere provided by or under this Act for such contravention, be punishable with fine which may extend to one hundred rupees.

MISCELLANEOUS (Sec 32-40)

OFFENCE BY COMPANIES, ETC (Sec 32)

Where a person committing an offence under this Act is a company, or other body corporate, or an association of persons (whether incorporated or not), every director, manager, secretary, agent or other officer or person concerned with the management thereof shall, unless he proves that the offence was committed without his knowledge or consent, be deemed to be guilty of such offence.

COMMENTS

This section talks of offences by companies under the Industrial Disputes Act, 1947; *Rabindra Chamria v. The Registrar of Companies (W.B.)*, (1992) 64 FLR 939 (SC).

CONDITIONS OF SERVICE, ETC., TO REMAIN UNCHANGED UNDER CERTAIN CIRCUMSTANCES DURING PENDENCY OF PROCEEDINGS (Sec 33)

- (1) During the pendency of any conciliation proceeding before a conciliation officer or a Board or of any proceeding before an arbitrator or a Labour Court or Tribunal or National Tribunal in respect of an industrial dispute, no employer shall—
 - (a) in regard to any matter connected with the dispute, alter, to the prejudice of the workmen concerned in such dispute, the conditions of service applicable to them immediately before the commencement of such proceeding; or
 - (b) for any misconduct connected with the dispute, discharge or punish, whether by dismissal or otherwise, any workman concerned in such dispute, save with the express permission in writing of the authority before which the proceeding is pending.
- (2) During the pendency of any such proceeding in respect of an industrial dispute, the employer may, in accordance with standing orders applicable to a workman concerned in such dispute or, where there are no such standing orders, in accordance with the terms of the contract, whether express or implied, between him and the workman:
 - (a) alter, in regard to any matter not connected with the dispute, the conditions of service applicable to that workman immediately before the commencement of such proceeding; or
 - (b) for any misconduct not connected with the dispute, discharge or punish, whether by dismissal or otherwise, that workman:

Provided that no such workman shall be discharged or dismissed, unless he has been paid wages for one month and an application has been made by the employer to the authority before which the proceeding is pending for approval of the action taken by the employer.
- (3) Notwithstanding Anything contained in sub-section (2), no employer shall, during the pendency of any such proceeding in respect of an industrial dispute, take any action against any protected workman concerned in such dispute :
 - (a) by altering, to the prejudice of such protected workman, the conditions of service applicable to him immediately before the commencement of such proceeding; or



- (b) by discharging or punishing, whether by dismissal or otherwise, such protected workman, save with the express permission in writing of the Authority before which the proceeding is pending.

Explanation : For the purposes of this sub-section, a “**protected workman**”, in relation to an establishment, means a workman who, being a member of the executive or other office-bearer of a registered trade union connected with the establishment, is recognised as such in accordance with rules made in this behalf.

- (4) In every establishment, the number of workmen to be recognised as protected workmen for the purposes of sub-section (3) shall be one per cent of the total number of workmen employed therein subject to a minimum number of five protected workmen and a maximum number of one hundred protected workmen and for the aforesaid purpose, the appropriate Government may make rules providing for the distribution of such protected workmen among various trade unions, if any, connected with the establishment and the manner in which the workmen may be chosen and recognised as protected workmen.
- (5) Where an employer makes an application to a conciliation officer, Board, an arbitrator, a Labour Court, Tribunal or National Tribunal under the proviso to sub-section (2) for approval of the action taken by him, the authority concerned shall, without delay, hear such application and pass, within a period of three months from the date of receipt of such application, such order in relation thereto as it deems fit:

Provided that where any such authority considers it necessary or expedient so to do, it may, for reasons to be recorded in writing, extend such period by such further period as it may think fit:

Provided further that no proceedings before any such authority shall lapse merely on the ground that any period specified in this sub-section had expired without such proceedings being completed.

COMMENTS

- (i) Violation of the provisions of section 33 of the Act entitles the workman to file a complaint under section 33A thereof and makes the employer liable to be punished. It, however, does not automatically entitle the employee to claim re-instatement; *Kimti Lal v. State of Haryana*, 1994 LLR 212 (P&H).
- (ii) Where there are more than one unions in operation, every union will have to be given the representation; *Maharashtra State Road Transport Corporation v. The Conciliation Officer*, 1994 LLR 196 (Bom).
- (iii) If approval is not granted the order of dismissal or discharge shall not be operative and the employee concerned shall be deemed to be in service; *G.K. Sengupta v. Hindustan Construction Co. Ltd.*, 1994 LLR 550 (Bom).
- (iv) Permission should be refused if the Tribunal is satisfied that the management's action is not *bona fide* or that the principles of natural justice have been violated or that the material on the basis of which the management came to a certain conclusion would not justify any reasonable person in coming to such a conclusion; *G.K. Sengupta v. Hindustan Construction Co. Ltd.*, 1994 LLR 550 (Bom).

SPECIAL PROVISION FOR ADJUDICATION AS TO WHETHER CONDITIONS OF SERVICE, ETC., CHANGED DURING PENDENCY OF PROCEEDING (Sec 33A)

Where an employer contravenes the provisions of section 33 during the pendency of proceedings before a conciliation officer, Board, an arbitrator, Labour Court, Tribunal or National Tribunal any employee aggrieved by such contravention, may make a complaint in writing, in the prescribed manner,

- (a) to such conciliation officer or Board, and the conciliation officer or Board shall take such complaint into account in mediating in, and promoting the settlement of, such industrial dispute; and
- (b) to such arbitrator, Labour Court, Tribunal or National Tribunal and on receipt of such complaint, the arbitrator, Labour Court, Tribunal or National

Tribunal, as the case may be, shall adjudicate upon the complaint as if it were a dispute referred to or pending before it, in accordance with the provisions of this Act and shall submit his or its award to the appropriate Government and the provisions of this Act shall apply accordingly.

COMMENTS

Conditions laid down in section 33A are preliminary and collateral upon which jurisdiction of the Industrial Tribunal depends; *Management of Dainik Naveen Duniya v. Presiding Officer, Labour Court*, (1991) 63 FLR 9 (MP).



POWER TO TRANSFER CERTAIN PROCEEDINGS (Sec 33B)

- (1) The appropriate Government may, by order in writing and for reasons to be stated therein, withdraw any proceeding under this Act pending before a Labour Court, Tribunal or National Tribunal and transfer the same to another Labour Court, Tribunal or National Tribunal, as the case may be, for the disposal of the proceeding and the Labour Court, Tribunal or National Tribunal to which the proceeding is so transferred may, subject to special directions in the order of transfer, proceed either *de novo* or from the stage at which it was so transferred:

Provided that where a proceeding under section 33 or section 33A is pending before a Tribunal or National Tribunal, the proceeding may also be transferred to a Labour Court.

- (2) Without prejudice to the provisions of sub-section (1), any Tribunal or National Tribunal, if so authorised by the appropriate Government, may transfer any proceeding under section 33 or section 33A pending before it to any one of the Labour Courts specified for the disposal of such proceedings by the appropriate Government by notification in the Official Gazette and the Labour Court to which the proceeding is so transferred shall dispose of the same.

COMMENTS

The Labour Court has no jurisdiction *suo motu* to transfer the proceedings to any other court; *Bennett Coleman & Co. Ltd. v. State of Punjab*, (1992) 64 FLR 449 (P&H).

RECOVERY OF MONEY DUE FROM AN EMPLOYER (Sec 33C)

- (1) Where any money is due to a workman from an employer under a settlement or an award or under the provisions of Chapter VA or Chapter VB the workman himself or any other person authorised by him in writing in this behalf, or, in the case of the death of the workman, his assignee or heirs may, without prejudice to any other mode of recovery, make an application to the appropriate Government for the recovery of the money due to him, and if the appropriate Government is satisfied that any money is so due, it shall issue certificate for that amount to the Collector who shall proceed to recover the same in the same manner as an arrear of land revenue :

Provided that every such application shall be made within one year from the date on which the money became due to the workman from the employer:

Provided further that any such application may be entertained after the expiry of the said period of one year, if the appropriate Government is satisfied that the applicant had sufficient cause for not making the application within the said period.

- (2) Where any workman is entitled to receive from the employer any money or any benefit which is capable of being computed in terms of money and if any question arises as to the amount of money due or as to the amount at which such benefit should be computed, then the question may, subject to any rules that may be made under this Act, be decided by such Labour Court as may be specified in this behalf by the appropriate Government within a period not exceeding three months.

Provided that where the presiding officer of a Labour Court considers it necessary or expedient so to do, he may, for reasons to be recorded in writing, extend such period by such further period as he may think fit.

- (3) For the purposes of computing the money value of a benefit, the Labour Court may, if it so thinks fit, appoint a Commissioner who shall, after taking such evidence as may be necessary, submit a report to the Labour Court and the Labour Court shall determine the amount after considering the report of the Commissioner and other circumstances of the case.
- (4) The decision of the Labour Court shall be forwarded by it to the appropriate Government and any amount found due by the Labour Court may be recovered in the manner provided for in sub-section (1).
- (5) Where workmen employed under the same employer are entitled to receive from him any money or any benefit capable of being computed in terms of money, then, subject to such rules as may be made in this behalf, a single application for the recovery of the amount due may be made on behalf of or in respect of any number of such workmen.

Explanation : In this section “Labour Court” includes any court constituted under any law relating to investigation and settlement of industrial disputes in force in any State.

**COMMENTS**

- (i) The cause of action created in favour of workman under section 33C (2) of the Act should in normal circumstances survive to the heirs; *Rameshwar Manjhi (deceased) through his son Lakhiram Manjhi v. The Management of Sungramgarh Colliery*, 1994 LLR 241 (SC).
- (ii) The proceedings under section 33C (2) are in the nature of execution proceedings and once it is shown that the relationship of master and servant has come to an end, rightly or wrongly, it is not open to the Labour Court to proceed on the basis that it still exists and commute the monetary benefits to which the workman may, in the event, be entitled to; *Canara Bank v. Presiding Officer*, 1994 LLR 189 (P&H).
- (iii) Once there is an admission of the existing right of the workman by the employer in regard to the benefit which the former is entitled to and receive from the latter, section 33C (2) of the Act would come into play; *M.D., Oswal Hosiery (Regd.) v. D.D. Gupta*, 1994 LLR 487 (Del).

COGNIZANCE OF OFFENCES (Sec 34)

- (1) No court shall take cognizance of any offence punishable under this Act or of the abetment of any such offence, save on complaint made by or under the authority of the appropriate Government.
- (2) No court inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of the first class shall try any offence punishable under this Act.

COMMENTS

- (i) A complaint for an offence under the Industrial Disputes Act can be filed by the appropriate Government or at its instance; *Tubu Enterprises Ltd. v. The Lt. Governor of Delhi*, 1994 LLR 169 (Delhi) (DB).
- (ii) Under section 34 of the Act the complaint for an offence thereunder, except section 30, cannot be filed by a private individual under the authority of the appropriate Government; *Tubu Enterprises Ltd. v. The Lt. Governor of Delhi*, 1994 LLR 169 (Del) (DB).

PROTECTION OF PERSONS (Sec 35)

- (1) No person refusing to take part or to continue to take part in any strike or lock-out which is illegal under this Act shall, by reason of such refusal or by reason of any action taken by him under this section, be subject to expulsion from any trade union or society, or to any fine or penalty, or to deprivation of any right or benefit to which he or his legal representatives would otherwise be entitled, or be liable to be placed in any respect, either directly or indirectly, under any disability or at any disadvantage as compared with other members of the union or society, anything to the contrary in the rules of a trade union or society notwithstanding.
- (2) Nothing in the rules of a trade union or society requiring the settlement of disputes in any manner shall apply to any proceeding for enforcing any right or exemption secured by this section, and in any such proceeding the Civil Court may, in lieu of ordering a person who has been expelled from membership of a trade union or society to be restored to membership, order that he be paid out of the funds of the trade union or society such sum by way of compensation or damages as that Court thinks just.

REPRESENTATION OF PARTIES (Sec 36)

- (1) A workman who is a party to dispute shall be entitled to be represented in any proceeding under this Act by
 - (a) any member of the executive or other office-bearer of a registered trade union of which he is a member;
 - (b) any member of the executive or other office-bearer of a federation of trade unions to which the trade union referred to in clause (a) is affiliated;
 - (c) where the worker is not a member of any trade union, by any member of the executive or other office-bearer of any trade union connected with, or by any other workman employed in, the industry in which the worker is employed and authorised in such manner as may be prescribed.
- (2) An employer who is a party to a dispute shall be entitled to be represented in any proceeding under this Act by—



- (a) an officer of an association of employers of which he is a member;
 - (b) an officer of a federation of association of employers to which the association referred to in clause (a) is affiliated;
 - (c) where the employer is not a member of any association of employers, by an officer of any association of employers connected with, or by any other employer engaged in, the industry in which the employer is engaged and authorised in such manner as may be prescribed.
- (3) No party to a dispute shall be entitled to be represented by a legal practitioner in any conciliation proceedings under this Act or in any proceedings before a court.
 - (4) In any proceeding before a Labour Court, Tribunal or National Tribunal, a party to a dispute may be represented by a legal practitioner with the consent of the other parties to the proceeding and with the leave of the Labour Court, Tribunal or National Tribunal, as the case may be.

COMMENTS

- (i) To practice is not an absolute right of any lawyer; *J. Subash v. Labour Court*, (1992) 65 FLR 561 (Ker).
- (ii) Taking the *vakalatnama* and keeping it on record cannot be taken as implied leave of the court or Tribunal; *Punjabi Ghasitaram Halwai v. Sahdeo Shivram Pauer*, (1994) 68 FLR 528 (Bom).
- (iii) Before a Labour Court or Industrial Tribunal, workman can be represented by an Executive or office-bearer of the Trade Union while the employer can be represented by the association of employers or its executive. The management has officers like Deputy Manager (Law), Assistant Manager (Law), etc., who are qualified law graduates. The Management is competent to engage any one of them to defend their case against one of their own workmen. However, employer is justified in approaching the Federation of Chamber of Commerce to contest a case of a workman of its own corporation; *R.M. Duraiswamy v. Labour Courts, Salem*, 1998 LLR 478 (16).

POWER TO REMOVE DIFFICULTIES (Sec 36A)

- (1) If, in the opinion of the appropriate Government, any difficulty or doubt arises as to the interpretation of any provision of an award or settlement, it may refer the question to such Labour Court, Tribunal or National Tribunal as it may think fit.
- (2) The Labour Court, Tribunal or National Tribunal to which such question is referred shall, after giving the parties an opportunity of being heard, decide such question and its decision shall be final and binding on all such parties.

POWER TO EXEMPT (Sec 36B)

Where the appropriate Government is satisfied in relation to any industrial establishment or undertaking or any class of industrial establishments or undertakings carried on by a department of that Government that adequate provisions exist for the investigation and settlement of industrial disputes in respect of workmen employed in such establishment or undertaking or class of establishments or undertakings, it may, by notification in the Official Gazette, exempt, conditionally or unconditionally such establishment or undertaking or class of establishments or undertakings from all or any of the provisions of this Act.

PROTECTION OF ACTION TAKEN UNDER THE ACT (Sec 37)

No suit, prosecution or other legal proceeding shall lie against any person for anything which is in good faith done or intended to be done in pursuance of this Act or any rules made thereunder.

POWER TO MAKE RULES (Sec 38)

- (1) The appropriate Government may, subject to the condition of previous publication, make rules for the purpose of giving effect to the provisions of this Act.
- (2) In particular and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:
 - (a) the powers and procedure of conciliation officers, Boards, Courts, Labour Courts, Tribunals and National Tribunals including rules as to the summoning of witnesses, the production of documents relevant to the subject-matter of an inquiry or investigation, the number of members necessary to form a quorum and the manner of submission of reports and awards;



- (aa) the form of arbitration agreement, the manner in which it may be signed by the parties the manner in which a notification may be issued under sub-section (3A) of section 10A, the powers of the arbitrator named in the arbitration agreement and the procedure to be followed by him;
 - (aaa) the appointment of assessors in proceedings under this Act;
 - (b) the constitution and functions of and the filling of vacancies in Works Committees, and the procedure to be followed by such Committees in the discharge of their duties;
 - (c) the allowances admissible to members of court and Boards and presiding officers of Labour Courts, Tribunals and National Tribunals and to assessors and witnesses;
 - (d) the ministerial establishment which may be allotted to a court, Board, Labour Court, Tribunal or National Tribunal and the salaries and allowances payable to members of such establishment;
 - (e) the manner in which and the persons by and to whom notice of strike or lock-out may be given and the manner in which such notices shall be communicated;
 - (f) the conditions subject to which parties may be represented by legal practitioners in proceedings under this Act before a court, Labour Court, Tribunal or National Tribunal;
 - (g) any other matter which is to be or may be prescribed.
- (3) Rules made under this section may provide that a contravention thereof shall be punishable with fine not exceeding fifty rupees.
- (4) All rules made under this section shall, as soon as possible after they are made, be laid before the State Legislature or, where the appropriate Government is the Central Government, before both Houses of Parliament.
- (5) Every rule made by the Central Government under this section 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 TO AMEND SCHEDULES (Sec 40)

- (1) The appropriate Government may, if it is of opinion that it is expedient or necessary in the public interest so to do, by notification in the Official Gazette, add to the First Schedule any industry, and on any such notification being issued, the First Schedule shall be deemed to be amended accordingly.
- (2) The Central Government may, by notification in the Official Gazette, add to or alter or amend the Second Schedule or the Third Schedule and on any such notification being issued, the Second Schedule or the Third Schedule, as the case may be, shall be deemed to be amended accordingly.
- (3) Every such notification shall, as soon as possible after it is issued, be laid before the Legislature of the State, if the notification has been issued by a State Government, or before Parliament, if the notification has been issued by the Central Government.

THE FIRST SCHEDULE

See Section 2(n)(vi)

Industries which may be declared to be Public Utility Services under sub-clause (vi) of clause (n) of section 2

- 1. Transport (other than railways) for the carriage of passengers or goods, by land or water;
- 2. Banking;
- 3. Cement;
- 4. Coal;
- 5. Cotton textiles;
- 6. Food stuffs;
- 7. Iron and Steel;



8. Defence establishments;
9. Service in hospitals and dispensaries;
10. Fire Brigade Service;
11. India Government Mints;
12. India Security Press;
13. Copper Mining;
14. Lead Mining;
15. Zinc Mining;
16. Iron Ore Mining;
17. Service in any oilfield;
19. Service in the Uranium Industry;
20. Pyrites Mining; 21. Security Paper Mill, Hoshangabad;
22. Services in the Bank Note Press, Dewas;
23. Phosphorite Mining;
24. Magnesite Mining;
25. Currency Note Press;
26. Manufacture or production of mineral oil (crude oil), motor and aviation spirit, diesel oil, kerosene oil, fuel oil, diverse hydrocarbon oils and their blends including synthetic fuels, lubricating oils and the like;
27. Service in the International Airports Authority of India.
28. Industrial establishments manufacturing or producing Nuclear Fuel and components, Heavy Water and Allied Chemicals and Atomic Energy.

THE SECOND SCHEDULE

(See Section 7)

Matters within the Jurisdiction of Labour Courts

1. The propriety or legality of an order passed by an employer under the standing orders;
2. The application and interpretation of standing orders;
3. Discharge or dismissal of workmen including re-instatement of, or grant of relief to, workmen wrongfully dismissed;
4. Withdrawal of any customary concession or privilege;
5. Illegality or otherwise of a strike or lock-out; and
6. All matters other than those specified in the Third Schedule.

THE THIRD SCHEDULE

(See Section 7A)

Matters within the Jurisdiction of Industrial Tribunals

1. Wages, including the period and mode of payment;
2. Compensatory and other allowances;
3. Hours of work and rest intervals;
4. Leave with wages and holidays;
5. Bonus, profit sharing, provident fund and gratuity;
6. Shift working otherwise than in accordance with standing orders;
7. Classification by grades;
8. Rules of discipline;
9. Rationalisation;
10. Retrenchment of workmen and closure of establishment; and
11. Any other matter that may be prescribed.

**THE FOURTH SCHEDULE**

(See Section 9A)

Conditions of Service for change of which Notice is to be given

1. Wages, including the period and mode of payment;
2. Contribution paid, or payable, by the employer to any provident fund or pension fund or for the benefit of the workmen under any law for the time being in force;
3. Compensatory and other allowances;
4. Hours of work and rest intervals;
5. Leave with wages and holidays;
6. Starting alteration or discontinuance of shift working otherwise than in accordance with standing orders;
7. Classification by grades;
8. Withdrawal of any customary concession or privilege or change in usage;
9. Introduction of new rules of discipline, or alteration of existing rules, except in so far as they are provided in standing orders;
10. Rationalisation, standardisation or improvement of plant or technique which is likely to lead to retrenchment of workmen;
11. Any increases or reduction (other than casual) in the number of persons employed or to be employed in any occupation or process or department or shift, not occasioned by circumstances over which the employer has no control.

THE FIFTH SCHEDULE

See Section 2(ra)

Unfair Labour Practices**I. On the part of employers and trade unions of employers**

1. To interfere with, restrain from, or coerce, workmen in the exercise of their right to organise, form, join or assist a trade union or to engage in concerted activities for the purposes of collective bargaining or other mutual aid or protection, that is to say:
 - (a) Threatening workmen with discharge or dismissal, if they join a trade union;
 - (b) Threatening a lock-out or closure, if a trade union is organised;
 - (c) Granting wage increase to workmen at crucial periods of trade union organisation, with a view to undermining the efforts of the trade union organisation.
2. To dominate, interfere with or contribute support, financial or otherwise, to any trade union, that is to say:
 - (a) an employer taking an active interest in organising a trade union of his workmen; and
 - (b) an employer showing partiality or granting favour to one of several trade unions attempting to organise his workmen or to its members, where such a trade union is not a recognised trade union.
3. To establish employer sponsored trade unions of workmen.
4. To encourage or discourage membership in any trade union by discriminating against any workman, that is to say:
 - (a) discharging or punishing a workman, because he urged other workmen to join or organise a trade union;
 - (b) discharging or dismissing a workman for taking part in any strike (not being a strike which is deemed to be an illegal strike under this Act);
 - (c) changing seniority rating of workmen because of trade union activities;
 - (d) refusing to promote workmen to higher posts on account of their trade union activities;



- (e) giving unmerited promotions to certain workmen with a view to creating discord amongst other workmen, or to undermine the strength of their trade union;
 - (f) discharging office-bearers or active members of the trade union on account of their trade union activities.
5. To discharge or dismiss workmen
 - (a) by way of victimisation;
 - (b) not in good faith, but in the colourable exercise of the employer's rights;
 - (c) by falsely implicating a workman in a criminal case on false evidence or on concocted evidence;
 - (d) for patently false reasons;
 - (e) on untrue or trumped up allegations of absence without leave;
 - (f) in utter disregard of the principles of natural justice in the conduct of domestic enquiry or with undue haste;
 - (g) for misconduct of a minor or technical character, without having any regard to the nature of the particular misconduct or the past record or service of the workman, thereby leading to a disproportionate punishment.
 6. To abolish the work of a regular nature being done by workmen, and to give such work to contractors as a measure of breaking a strike.
 7. To transfer a workman *mala fide* from one place to another, under the guise of following management policy.
 8. To insist upon individual workmen, who are on a legal strike to sign a good conduct bond, as a pre-condition to allowing them to resume work.
 9. To show favouritism or partiality to one set of workers regardless of merit.
 10. To employ workmen as "*badlis*", casuals or temporaries and to continue them as such for years, with the object of depriving them of the status and privileges of permanent workmen.
 11. To discharge or discriminate against any workman for filing charges or testifying against an employer in any enquiry or proceeding relating to any industrial dispute.
 12. To recruit workmen during a strike which is not an illegal strike.
 13. Failure to implement award, settlement or agreement.
 14. To indulge in acts of force or violence.
 15. To refuse to bargain collectively, in good faith with the recognised trade unions.
 16. Proposing or continuing a lock-out deemed to be illegal under this Act.

II. On the part of workmen and trade unions of workmen

1. To advise or actively support or instigate any strike deemed to be illegal under this Act.
2. To coerce workmen in the exercise of their right to self-organisation or to join a trade union or refrain from joining any trade union, that is to say :
 - (a) for a trade union or its members to picketing in such a manner that non-striking workmen are physically debarred from entering the work places;
 - (b) to indulge in acts of force or violence or to hold out threats of intimidation in connection with a strike against non-striking workmen or against managerial staff.
3. For a recognised union to refuse to bargain collectively in good faith with the employer.
4. To indulge in coercive activities against certification of a bargaining representative.
5. To stage, encourage or instigate such forms of coercive actions as wilful "go slow", squatting on the work premises after working hours or "gherao" of any of the members of the managerial or other staff.
6. To stage demonstrations at the residences of the employers or the managerial staff members.
7. To incite or indulge in wilful damage to employer's property connected with the industry.



8. To indulge in acts of force or violence or to hold out threats of intimidation against any workman with a view to prevent him from attending work.

Find below a compilation of Frequently Asked Questions in Industrial Disputes Act.

1. What are Industrial Disputes?

Industrial Dispute means any dispute or differences between employers and employees or between employers and workmen or between workmen and workmen which is connected with the employment or non-employment or the terms of employment or with the conditions of labour of any person.

2. What are the different categories of Industrial Disputes?

The Second Schedule of the I.D. Act deals with matters within the jurisdiction of Labour Courts which fall under the category of Rights Disputes. Such disputes are as follows:

1. The propriety or legality of an order passed by an employer under the standing orders;
2. The application and interpretation of standing orders which regulate conditions of employment.
3. Discharge or dismissal of workmen including reinstatement of, or grant of relief to, workmen wrongfully dismissed;
4. Withdrawal of any customary concession or privilege;
5. Illegality or otherwise of a strike or lock-out; and
6. All matters other than those specified in the Third Schedule.

The Third Schedule of the I.D. Act deals with matters within the jurisdiction of Industrial Tribunals which could be classified as Interest Disputes. These are as follows:-

1. Wages, including the period and mode of payment;
2. Compensatory and other allowances;
3. Hours of work and rest intervals;
4. Leave with wages and holidays;
5. Bonus, profit sharing, provident fund and gratuity;
6. Shift working otherwise than in accordance with standing orders;
7. Classification by grades;
8. Rules of discipline;
9. Rationalization;
10. Retrenchment of workmen and closure of establishment; and
11. Any other matter that may be prescribed.

3. Who can raise an Industrial Dispute?

Any person who is a workman employed in an industry can raise an industrial dispute. A workman includes any person (including an apprentice) employed in an industry to do manual, unskilled, skilled, technical, operational, clerical or supervisory work for hire or reward. It excludes those employed in the Army, Navy, Air Force and in the police service, in managerial or administrative capacity. Industry means any business, trade, undertaking, manufacture or calling of employers and includes any calling, service, employment, handicraft, or industrial occupation or avocation of workmen.

4. How to raise an Industrial Dispute?

A workman can raise a dispute directly before a Conciliation Officer in the case of discharge, dismissal, retrenchment or any form of termination of service. In all other cases listed at 2 above, the dispute has to be raised by a Union / Management.

5. Who are Conciliation Officers and what do they do?

The Organization of the Chief Labour Commissioner(Central) acts as the primary conciliatory agency in the Central Government for industrial disputes. There are the Regional Labour Commissioners (Central) and Assistant Labour Commissioners (Central) who on behalf of the Chief Labour Commissioner (Central) act as Conciliatory Officers in different parts of the country. The Conciliation Officer make efforts to resolve the dispute through settlement between the workmen and the management. The duties of Conciliation Officers have been laid down under Section 12 of the Industrial Disputes Act.



6. What happens if conciliation fails?

In case of failure of conciliation (FOC) a report is sent to Government (IR Desks in Ministry of Labour). The Ministry of Labour after considering the FOC Report exercises the powers available to it under Section 10 of the Industrial Disputes Act and either refers the dispute for adjudication or refuses to do so. Details of functions of IR Desks and reasons for declining may be seen above.

There are at present 17 Central Government Industrial Tribunals-cum-Labour Courts in different parts of the country to whom industrial disputes could be referred for adjudication. These CGTIs-cum-Labour Courts are at New Delhi, Mumbai (2 CGITs), Bangalore, Kolkata, Asansol, Dhanbad (2 CGITs), Jabalpur, Chandigarh, Kanpur, Jaipur, Lucknow, Nagpur, Hyderabad, Chennai and Bhubaneshwar. Out of these CGITs, 2 CGITs namely Mumbai-I and Kolkata have been declared as National Industrial Tribunals.

7. What happens when the dispute is referred to Labour Court?

After the matter is referred to any of the CGIT- cum- Labour Court, the adjudication process begins. At the end of the proceedings an Award is given by the Presiding Officer.

The Ministry of Labour under Section 17 of the I.D. Act publishes the Award in the Official Gazette within a period of 30 days from the date of receipt of the Award.

8. How is the Award implemented? An Award becomes enforceable on the expiry of 30 days from the date of its publication in the Official Gazette. The Regional Labour Commissioner is the implementing authority of the Awards.

9. What are the provisions for General Prohibition of Strikes and Lockouts?

No workman who is employed in any industrial establishment shall go on strike in breach of contract and no employer of any such workman shall declare a lockout:

- (a) During the pendency of conciliation proceedings before a Board and seven days after the conclusion of such proceedings,
- (b) During the pendency of such proceedings before a Labour Court, Tribunal or National Tribunal and 2 months after the conclusion of such proceedings.
- (c) During the pendency of arbitration proceedings before an Arbitrator and 2 months after the conclusion of such proceedings, where a notification has been issued.
- (d) During any period during in which a settlement or Award is in operation in respect of any of the matters covered by the settlement or Award.

10. Does the workman have the Right to go on strike with proper notice in Public Utility Services?

No person employed in a Public Utility Service can go on strike without giving to the employer notice of strike;

- (a) Within 6 weeks before striking.
- (b) Within 14 days of giving such notice.
- (c) Before the expiry of the date of strike specified in such notice.
- (d) During the pendency of any conciliation proceedings before a Conciliation Officer and 7 days after the conclusion of such proceedings.

11. Does the Employer have the right to lock out any Public Utility Service?

No employer carrying on any Public Utility service can lockout any of his workman :

- (i) Without giving to them notice of lockout provided within 6 weeks before locking out.
- (ii) Within 14 days of giving such notice.
- (iii) Before expiry of the date of lockout specified in any such notice.
- (iv) During the pendency of any conciliation proceedings before a Conciliation Officer and 7 days after the conclusion of such proceedings.

12. What compensation will a workman get when laid off?

Whenever a workman (other than a badli workman or a casual workman) whose name is borne on the muster rolls of an industrial establishment employing 50 or more workmen on an average working day and who has completed not less than one year of continuous service under an employer laid off, whether



continuously or intermittently, he is to be paid by the employer for all days during which he is so laid off, except for such weekly holidays as may intervene, compensation which shall be equal to fifty per cent of the total of the basic wages and dearness allowance that would have been payable to him had he not been so laid-off.

13. What are the conditions precedent to retrenchment of workmen?

No workmen employed in any industry who has been in continuous service for not less than one year under an employer can be retrenched by that employer until :

- (a) The workman has to be given one month's notice in writing indicating the reasons for retrenchment or the workman has to be paid in lieu of such notice, wages for the period of the notice.
- (b) The workman has to be paid, at the time of retrenchment, compensation which is equivalent to fifteen days' average pay (for every completed year of continuous service) or any part thereof in excess of six months; and
- (c) Notice in the prescribed manner is to be served on the appropriate Government (or such authority as may be specified by the appropriate Government by notification in the Official Gazette).

14. What compensation will the workman get when an undertaking closes down?

Where an undertaking is closed down for any reason whatsoever, every workman who has been in continuous service for not less than one year in that undertaking immediately before such closure is entitled to notice and compensation in accordance with the provisions as if the workman had been retrenched.

Provided that where the undertaking is closed down on account of unavoidable circumstances beyond the control of the employer, the compensation to be paid to the workman is not to exceed his average pay for three months.



3.3 THE WORKMEN'S COMPENSATION ACT, 1923

INTRODUCTION

The passing of Workmen's Compensation Act in 1923 was the first step towards social security of workmen. The theory of this act is that "the cost of product should bear the blood of the workman". This Act provides compensation to certain classes of workmen by their employers for injury, which may be suffered, by the workmen as result of an accident during the course of employment.

Object

To provide Compensation to Workmen for accidental injury and occupational diseases arising during and in the course of employment.

Applicability of Act

This Act is applicable to all employments in which the ESI Act is not applicable.

BASIC CONCEPTS

"Dependent" means any of the following relatives of a deceased workman, namely :—

- (i) A widow, a minor legitimate or adopted son, and unmarried legitimate or adopted daughter, or a widowed mother; and
- (ii) If wholly dependent on the earnings of the workman at the time of his death, a son or a daughter who has attained the age of 18 years and who is infirm;
- (iii) If wholly or in part dependent on the earnings of the workman at the time of his death,
 - (a) a widower,
 - (b) A parent other than a widowed mother,
 - (c) A minor illegitimate son, an unmarried illegitimate daughter or a daughter legitimate or illegitimate or adopted if married and a minor or if widowed and a minor,
 - (d) A minor brother or an unmarried sister or a widowed sister if a minor,
 - (e) A widowed daughter-in-law,
 - (f) A minor child of a pre-deceased son,
 - (g) A minor child of a pre-deceased daughter where no parent of the child is alive, or
 - (h) A paternal grandparent if no parent of the workman is alive.

Explanation : For the purposes of sub-clause (ii) and items (f) and (g) of sub-clause (iii), references to a son, daughter or child include an adopted son, daughter or child respectively;

"Employer"

Includes any body of persons whether incorporated or not, and any managing agent of an employer, and the legal representative of a deceased employer, and, when the services of a workman are temporarily lent or let on hire to another person by the person with whom the workman has entered into a contract of service or apprenticeship, means such other person while the workman is working for him;

"Wages"

Includes any privilege or benefit which is capable of being estimated in money, other than a travelling allowance or the value of any travelling concession or a contribution paid by the employer a workman towards any pension or provident fund or a sum paid to a workman to cover any special expenses entailed on him by the nature of his employment;

"Workman"

Means any person (other than a person whose employment is of a casual nature and who is employed otherwise than for the purposes of the employer's trade or business) who is - (i) a railway servant as defined in clause (34) of section 2 of the Railways Act, 1989 (24 of 1989), not permanently employed in any administrative, district or sub-divisional office of a railway and not employed in any such capacity as is specified in Schedule II.

**Disablement**

Disablement means loss of capacity to work or to move. Disablement reduces a worker's earning capacity. Disablement may be partial or total. Further it may be temporary or permanent.

Partial disablement reduces the earning capacity of a workman as a result of some accident.

Temporary partial disablement reduces the earning capacity of a workman in the type of employment he was engaged in at the time of accident.

Permanent partial disablement reduces the earning capacity of a workman in every types of employment he was capable of at the time of accident.

Total disablement, whether temporary or permanent makes a workman incapable of performing all types of work as a result accident. He becomes unfit totally and is not able to get job anywhere due to disablement. Total disablement results from every injury specified in Part I Schedule I or from combination of injuries specified in Part II where aggregate loss of earning capacity amounts to 100%.

Main Provisions of the Act

Injury / Diseases arising out of and in course of employment are payable – The term 'arising out of and in the course of employment' means that Compensation is payable only in those injury/diseases where the employment is the immediate and proximate cause of the said injury/disease. In other words, the injury/disease would not have occurred had the workman not been employed in the particular employment.

Compensation payable – The Workmen's Compensation payable as per the act is as under :

Compensation :

1. Death due to injury 50% of wages * Relevant factor OR ` 80,000/- , whichever is more,
2. Permanent total disablement due to injury 60% of wages * Relevant factor OR ` 90,000/-, whichever is more,
3. Permanent Partial disablement due to injury % of compensation as is payable in (ii) or % of compensation proportionate to loss of earning capacity,
4. Temporary Disablement 25% of wages paid half monthly,
5. Occupational disease Occupational disease to be treated as injury by accident and compensation as applicable in the cases of injury are payable.

Following points are to be noted in calculation of compensation :

- (a) Wages to be actual or Max ` 4000/- per month,
- (b) Relevant factor are given in Schedule III of the Act,
- (c) Employee not eligible for compensation when he/she has filed a Civil Suit against the employer.

Compensation not payable : Compensation under this Act is not payable when

- The disablement due to injury is less than 4 days.
- The employee was under the influence of drugs/alcohol at the time of accident.
- Workman willfully disobeys any safety rule.
- Workman willfully removes/disregards any safety guard/ equipments.
- Workman has filed a Civil suit against the employer for claim of compensation.
- Workman has refused to get himself medically examined cost of which is borne by the employer.

Payment of Compensation

The Compensation payable under the Act is to be made by deposit to the Commissioner of Workmen's Compensation who will distribute the same to workmen or his dependents.

However, amount equal to 3 months wages can be paid directly to the dependents in cases of death of workman, provided the said amount is less than the total compensation payable to workman.

Report of death and serious bodily injury – should be given within 7 days of the death/ serious bodily injury to the Commissioner of Workmen's Compensation.



Medical Examination –The employer should get the medical examination of the workman who has made a claim for compensation, within 3 days of receipt of claim.

Workmen's Compensation Rules, 1924:

Object:

The objective of this Act is that in the case of an employment injury compensation be provided to the injured workman and in case of his death to his dependants.

Employer to pay compensation:

In case a personal injury is caused to a workman by accident arising out of and in the course of his employment, his employer is liable to pay compensation in accordance with the provision of the Act within 30 days from the date when it fell due otherwise he would also be liable to pay interest and penalty.

When employer is not liable:

In case the disablement of workman is three or less days; except in case of death when the injury is caused due to influence of drink or drug taken by the workman or upon his wilful disobedience to obey safety rules or removal of safetyguards by him.

Amount of compensation :

- (1) in case of death:- an amount equal to 50% of the monthly wage multiplied by the relevant factor as given in Schedule IV of the Act or ` 80,000/-whichever is more.
- (2) In case of permanent total disablement, it is 60% or ` 90,000/-whichever is more, and
- (3) In case of permanent partial disablement occurs then the compensation is proportionate to the disability arrived as at (2) above.

Notice : An injured person or his dependants have to give a notice to the employer to pay compensation.

Claim :

Upon the failure or refusal of an employer to give compensation, an application is to be made in Form - F to the Commissioner under the Workmen's Compensation Act, 1923 who is the Assistant Labour Commissioner or the Labour-cum-Conciliation Officer of the area where the accident took place or where the claimant ordinarily resides or where the employer has his registered office. After hearing both the parties, the Commissioner decides the claim.

Contracting out: Any contract or agreement whereby an injured person or his dependant relinquishes or reduces his right to receive compensation is null and void to that extent.

Appeal :

An appeal lies to the High Court against the orders of the Commissioner with regard to the awarding or refusing to award compensation, or imposing interest or penalty, or regarding distribution of compensation etc. Recovery : The amount of compensation awarded by the Commissioner is to be recovered as arrears of land revenue.

EMPLOYER'S LIABILITY FOR COMPENSATION (Sec 3)

- (1) If personal injury is caused to a workman by accident arising out of and in the course of his employment, his employer shall be liable to pay compensation in accordance with the provisions of this Chapter :

Provided that the employer shall not be so liable—

- (a) in respect of any injury which does not result in the total or partial disablement of the workman for a period exceeding three days;
- (b) in respect of any injury, not resulting in death or permanent total disablement, caused by an accident which is directly attributable to—
 - (i) the workman having been at the time thereof under the influence of drink or drugs, or
 - (ii) the wilful disobedience of the workman to an order expressly given, or to a rule expressly framed, for the purpose of securing the safety of workmen, or
 - (iii) the wilful removal or disregard by the workman of any safety guard or other device which he knew to have been provided for the purpose of securing the safety of workmen.
- (2) If a workman employed in any employment specified in Part A of Schedule III contracts any disease specified therein as an occupational disease peculiar to that employment, or if a workman, whilst in the



service of an employer in whose service he has been employed for a continuous period of not less than six months (which period shall not include a period of service under any other employer in the same kind of employment) in any employment specified in Part B of Schedule III, contracts any disease specified therein as an occupational disease peculiar to that employment, or if a workman whilst in the service of one or more employers in any employment specified in Part C of Schedule III, for such continuous period as the Central Government may specify in respect of each such employment, contracts any disease specified therein as an occupational disease peculiar to that employment, the contracting of the disease shall be deemed to be an injury by accident within the meaning of this section and, unless the contrary is proved, the accident shall be deemed to have arisen out of, and in the course of, the employment :

Provided that if it is proved,—

- (a) that a workman whilst in the service of one or more employers in any employment specified in Part C of Schedule III has contracted a disease specified therein as an occupational disease peculiar to that employment during a continuous period which is less than the period specified under this sub-section for that employment, and
- (b) that the disease has arisen out of and in the course of the employment; the contracting of such disease shall be deemed to be an injury by accident within the meaning of this section :

Provided further that if it is proved that a workman who having served under any employer in any employment specified in Part B of Schedule III or who having served under one or more employers in any employment specified in Part C of that Schedule, for a continuous period specified under this sub-section for that employment and he has after the cessation of such service contracted any disease specified in the said Part B or the said Part C, as the case may be, as an occupational disease peculiar to the employment and that such disease arose out of the employment, the contracting of the disease shall be deemed to be an injury by accident within the meaning of this section.

- (2A) If a workman employed in any employment specified in Part C of Schedule III contracts any occupational disease peculiar to that employment, the contracting whereof is deemed to be an injury by accident within the meaning of this section, and such employment was under more than one employer, all such employers shall be liable for the payment of the compensation in such proportion as the Commissioner may, in the circumstances, deem just.
- (3) The Central Government or the State Government, after giving, by notification in the Official Gazette, not less than three months' notice of its intention so to do, may, by a like notification, add any description of employment to the employments specified in Schedule III, and shall specify in the case of employments so added the diseases which shall be deemed for the purposes of this section to be occupational diseases peculiar to those employments respectively, and thereupon the provisions of sub-section (2) shall apply. In the case of a notification by the Central Government, within the territories to which this Act extends or, in case of a notification by the State Government, within the State as if such diseases had been declared by this Act to be occupational diseases peculiar to those employments.
- (4) Save as provided by Sub-sections (2), (2A) and (3), no compensation shall be payable to a workman in respect of any disease unless the disease is directly attributable to a specific injury by accident arising out of and in the course of his employment.
- (5) Nothing herein contained shall be deemed to confer any right to compensation on a workman in respect of any injury if he has instituted in a Civil Court a suit for damages in respect of the injury against the employer or any other person; and no suit for damages shall be maintainable by a workman in any Court of law in respect of any injury -
 - (a) If he has instituted a claim to compensation in respect of the injury before a Commissioner; or
 - (b) If an agreement has been come to between the workman and his employer providing for the payment of compensation in respect of the injury in accordance with the provisions of this Act.

AMOUNT OF COMPENSATION (Sec 4)

- (1) Subject to the provisions of this Act, the amount of compensation shall be as follows, namely:—
 - (a) Where death results from the injury, an amount equal to fifty percent of the monthly wages of the deceased workman multiplied by the relevant factor; or an amount of fifty thousand rupees, whichever is more;



- (b) Where permanent total disablement results from the injury, an amount equal to sixty percent of the monthly wages of the injured workman multiplied by the relevant factor, or an amount of sixty thousand rupees, whichever is more.

Explanation I : For the purposes of clause (a) and clause (b), “relevant factor”, in relation to a workman means the factor specified in the second column of Schedule IV against the entry in the first column of that Schedule specifying the number of years which are the same as the completed years of the age of the workman on his last birthday immediately preceding the date on which the compensation fell due;

Explanation II : Where the monthly wages of a workman exceed two thousand rupees, his monthly wages for the purposes of clause (a) and clause (b) shall be deemed to be two thousand rupees only;

- (c) Where permanent partial disablement results from the injury —
- (i) in the case of an injury specified in Part II of Schedule I, such percentage of the compensation which would have been payable in the case of permanent total disablement as is specified therein as being the percentage of the loss of earning capacity caused by that injury, and
- (ii) In the case of an injury not specified in Schedule I, such percentage of the compensation payable in the case of permanent total disablement as is proportionate to the loss of earning capacity (as assessed by the qualified medical practitioner) permanently caused by the injury;

Explanation I : Where more injuries than one are caused by the same accident, the amount of compensation payable under this head shall be aggregated but not so in any case as to exceed the amount which would have been payable if permanent total disablement had resulted from the injuries;

Explanation II : In Assessing the loss of earning capacity for the purposes of sub-clause (ii) the qualified medical practitioner shall have due regard to the percentages of loss of earning capacity in relation to different injuries specified in Schedule I;

- (d) Where temporary a half monthly payment of the sum disablement, whether equivalent to twenty-five per cent of total or partial, results monthly wages of the workman, to from the injury be paid in accordance with the provisions of sub-section (2).
- (1A) Notwithstanding anything contained in sub-section (1), while fixing the amount of compensation payable to a workman in respect of an accident occurred outside India, the Commissioner shall take into account the amount of compensation, if any, awarded to such workman in accordance with the law of the country in which the accident occurred and shall reduce the amount fixed by him by the amount of compensation awarded to the workman in accordance with the law of that country.
- (2) The half-monthly payment referred to in clause (d) of sub-section (1) shall be payable on the sixteenth day—
- (i) From the date of disablement where such disablement lasts for a period of twenty-eight days or more; or
- (ii) After the expiry of a waiting period of three days from the date of disablement where such disablement lasts for a period of less than twenty-eight days; and thereafter half-monthly during the disablement or during a period of five years, whichever period is shorter :

Provided that—

- (a) there shall be deducted from any lump sum or half-monthly payments to which the workman is entitled the amount of any payment or allowance which the workman has received from the employer by way of compensation during the period of disablement prior to the receipt of such lump sum or of the first half-monthly payment, as the case may be; and
- (b) No half-monthly payment shall in any case exceed the amount, if any, by which half the amount of the monthly wages of the workman before the accident exceeds half the amount of such wages which he is earning after the accident.

Explanation : Any payment or allowance which the workman has received from the employer towards his medical treatment shall not be deemed to be a payment or allowance received by him by way of compensation within the meaning of clause (a) of the proviso.

- (3) On the ceasing of the disablement before the date on which any half-monthly payment falls due, there shall be payable in respect of that half-month a sum proportionate to the duration of the disablement in that half-month.



- (4) If the injury of the workman results in his death, the employer shall, in addition to the compensation under sub-section (1), deposit with the Commissioner a sum of one thousand rupees for payment of the same to the eldest surviving dependant of the workman towards the expenditure of the funeral of such workman or where the workman did not have a dependant or was not living with his dependant at the time of his death to the person who actually incurred such expenditure.

COMPENSATION TO BE PAID WHEN DUE AND PENALTY FOR DEFAULT (Sec 4A)

- (1) Compensation under section 4 shall be paid as soon as it falls due.
- (2) In cases where the employer does not accept the liability for compensation to the extent claimed, he shall be bound to make provisional payment based on the extent of liability which he accepts, and, such payment shall be deposited with the Commissioner or made to the workman, as the case may be, without prejudice to the right of the workman to make any further claim.
- (3) Where any employer is in default in paying the compensation due under this Act within one month from the date it fell due, the Commissioner shall —
- (a) direct that the employer shall, in addition to the amount of the arrears, pay simple interest thereon at the rate of twelve per cent per annum or at such higher rate not exceeding the maximum of the lending rates of any scheduled bank as may be specified by the Central Government, by notification in the Official Gazette, on the amount due; and
- (b) if, in his opinion, there is no justification for the delay, direct that the employer shall, in addition to the amount of the arrears and interest thereon, pay a further sum not exceeding fifty per cent of such amount by way of penalty :

Provided that an order for the payment of penalty shall not be passed under clause (b) without giving a reasonable opportunity to the employer to show cause why it should not be passed.

Explanation : For the purposes of this sub-section, “scheduled bank” means a bank for the time being included in the Second Schedule to the Reserve Bank of India Act, 1934 (2 of 1934).

- (3A) The interest payable under sub-section (3) shall be paid to the workman or his dependant, as the case may be, and the penalty shall be credited to the State Government.

METHOD OF CALCULATING WAGES (Sec 5)

In this Act and for the purposes thereof the expression “monthly wages” means the amount of wages deemed to be payable for a month’s service (whether the wages are payable by the month or by whatever other period or at piece rates), and calculated as follows, namely :—

- (a) where the workman has, during a continuous period of not less than twelve months immediately preceding the accident, been in the service of the employer who is liable to pay compensation, the monthly wages of the workman shall be one-twelfth of the total wages which have fallen due for payment to him by the employer in the last twelve months of that period;
- (b) where the whole of the continuous period of service immediately preceding the accident during which the workman was in the service of the employer who is liable to pay the compensation was less than one month, the monthly wages of the workman shall be the average monthly amount which, during the twelve months immediately preceding the accident, was being earned by a workman employed on the same work by the same employer, or, if there was no workman so employed, by a workman employed on similar work in the same locality;
- (c) in other cases [including cases in which it is not possible for want of necessary information to calculate the monthly wages under clause (b), the monthly wages shall be thirty times the total wages earned in respect of the last continuous period of service immediately preceding the accident from the employer who is liable to pay compensation, divided by the number of days comprising such period.

Explanation : A period of service shall, for the purposes of this section be deemed to be continuous which has not been interrupted by a period of absence from work exceeding fourteen days.

REVIEW (Sec 6)

- (1) Any half-monthly payment payable under this Act, either under an agreement between the parties or under the order of a Commissioner, may be reviewed by the Commissioner, on the application either of



the employer or of the workman accompanied by the certificate of a qualified medical practitioner that there has been a change in the condition of the workman or, subject to rules made under this Act, on application made without such certificate.

- (2) Any half-monthly payment may, on review under this section, subject to the provisions of this Act, be continued, increased, decreased or ended, or if the accident is found to have resulted in permanent disablement, be converted to the lump sum to which the workman is entitled less any amount which he has already received by way of half-monthly payments.

COMMUTATION OF HALF-MONTHLY PAYMENTS (Sec 7)

Any right to receive half-monthly payments may, by agreement between the parties or, if the parties cannot agree and the payments have been continued for not less than six months, on the application of either party to the Commissioner be redeemed by the payment of a lump sum of such amount as may be agreed to by the parties or determined by the Commissioner, as the case may be.

DISTRIBUTION OF COMPENSATION (Sec 8)

- (1) No payment of compensation in respect of a workman whose injury has resulted in death, and no payment of a lump sum as compensation to a woman or a person under a legal disability, shall be made otherwise than by deposit with the Commissioner, and no such payment made directly by an employer shall be deemed to be a payment of compensation :

Provided that, in the case of a deceased workman, an employer may make to any dependant advances on account of compensation of an amount equal to three months' wages of such workman and so much of such amount as does not exceed the compensation payable to that dependant shall be deducted by the Commissioner from such compensation and repaid to the employer.

- (2) Any other sum amounting to not less than ten rupees which is payable as compensation may be deposited with the Commissioner on behalf of the person entitled thereto.
- (3) The receipt of the Commissioner shall be a sufficient discharge in respect of any compensation deposited with him.
- (4) On the deposit of any money under sub-section (1), as compensation in respect of a deceased workman the Commissioner shall, if he thinks necessary, cause notice to be published or to be served on each dependant in such manner as he thinks fit, calling upon the dependants to appear before him on such date as he may fix for determining the distribution of the compensation.

If the Commissioner is satisfied after any inquiry which he may deem necessary, that no dependant exists, he shall repay the balance of the money to the employer by whom it was paid.

The Commissioner shall, on application by the employer, furnish a statement showing in detail all disbursements made.

- (5) Compensation deposited in respect of a deceased workman shall, subject to any deduction made under sub-section (4), be apportioned among the dependants of the deceased workman or any of them in such proportion as the Commissioner thinks fit, or may, in the discretion of the Commissioner, be allotted to any one dependant.
- (6) Where any compensation deposited with the Commissioner is payable to any person, the Commissioner shall, if the person to whom the compensation is payable is not a woman or a person under a legal disability, and may, in other cases, pay the money to the person entitled thereto.
- (7) Where any lump sum deposited with the Commissioner is payable to a woman or a person under a legal disability, such sum may be invested, applied or otherwise dealt with for the benefit of the woman, or of such person during his disability, in such manner as the Commissioner may direct; and where a half-monthly payment is payable to any person under a legal disability, the Commissioner may, of his own motion or on an application made to him in this behalf, order that the payment be made during the disability to any dependant of the workman or to any other person, whom the Commissioner thinks best fitted to provide for the welfare of the workman.
- (8) Where, on application made to him in this behalf or otherwise, the Commissioner is satisfied that, on account of neglect of children on the part of a parent or on account of the variation of the circumstances of any dependant or for any other sufficient cause, an order of the Commissioner as to the distribution of



any sum paid as compensation or as to the manner in which any sum payable to any such dependant is to be invested, applied or otherwise dealt with, ought to be varied, the Commissioner may make such orders for the variation of the former order as he thinks just in the circumstances of the case :

Provided that no such order prejudicial to any person shall be made unless such person has been given an opportunity of showing cause why the order should not be made, or shall be made in any case in which it would involve the repayment by a dependant of any sum already paid to him.

- (9) Where the Commissioner varies any order under sub-section (8) by reason of the fact that payment of compensation to any person has been obtained by fraud, impersonation or other improper means, any amount so paid to or on behalf of such person may be recovered in the manner hereinafter provided in section 31.

COMPENSATION NOT TO BE ASSIGNED, ATTACHED OR CHARGED (Sec 9)

Save as provided by this Act, no lump sum or half-monthly payment payable under this Act shall in-any way be capable of being assigned or charged or be liable to attachment or pass to any person other than the workman by operation of law, nor shall any claim be set off against the same.

NOTICE AND CLAIM (Sec 10)

- (1) No claim for compensation shall be entertained by a Commissioner unless notice of the accident has been given in the manner hereinafter provided as soon as practicable after the happening thereof and unless the claim is preferred before him within two years of the occurrence of the accident or, in case of death, within two years from the date of death :

Provided that, where the accident is the contracting of a disease in respect of which the provisions of sub-section (2) of section 3 are applicable, the accident shall be deemed to have occurred on the first of the days during which the workman was continuously absent from work in consequence of the disablement caused by the disease :

Provided further that in case of partial disablement due to the contracting of any such disease and which does not force the workman to absent himself from work, the period of two years shall be counted from the day the workman gives notice of the disablement to his employer :

Provided further that if a workman who, having been employed in an employment for a continuous period, specified under sub-section (2) of section 3 in respect of that employment, ceases to be so employed and develops symptoms of an occupational disease peculiar to that employment within two years of the cessation of employment, the accident shall be deemed to have occurred on the day on which the symptoms were first detected:

Provided further that the want of or any defect or irregularity in a notice shall not be a bar to the entertainment of a claim - (a) if the claim is preferred in respect of the death of a workman resulting from an accident which occurred on the premises of the employer, or at any place where the workman at the time of the accident was working under the control of the employer or of any person employed by him, and the workman died on such premises or at such place, or on any premises belonging to the employer, or died without having left the vicinity of the premises or place where the accident occurred, or (b) if the employer or any one of several employers or any person responsible to the employer for the management of any branch of the trade or business in which the injured workman was employed had knowledge of the accident from any other source at or about the time when it occurred :

Provided further that the Commissioner may entertain and decide any claim to compensation in any case notwithstanding that the notice has not been given, or the claim has not been preferred in due time as provided in this sub-section, if he is satisfied that the failure so to give the notice or prefer the claim, as the case may be, was due to sufficient cause.

- (2) Every such notice shall give the name and address of the person injured and shall state in ordinary language the cause of the injury and the date on which the accident happened, and shall be served on the employer or upon any one of several employers, or upon any person responsible to the employer for the management of any branch of the trade or business in which the injured workman was employed.
- (3) The State Government may require that any prescribed class of employers shall maintain at their premises at which workmen are employed a notice-book, in the prescribed form, which shall be readily accessible at all reasonable times to any injured workman employed on the premises and to any person acting bond fide on his behalf.



- (4) A notice under this section may be served by delivering it at, or sending it by registered post addressed to, the residence or any office or place of business of the person on whom it is to be served, or, where a notice-book is maintained, by entry in the notice book.

POWER TO REQUIRE FROM EMPLOYERS STATEMENTS REGARDING FATAL ACCIDENTS (Sec 10A)

- (1) Where a Commissioner receives information from any source that a workman has died as a result of an accident arising out of and in the course of his employment, he may send by registered post a notice to the workman's employer requiring him to submit within thirty days of the service of the notice, a statement, in the prescribed form, giving the circumstances attending the death of the workman, and indicating whether, in the opinion of the employer, he is or is not liable to deposit compensation on account of the death.
- (2) If the employer is of opinion that he is liable to deposit compensation, he shall make the deposit within thirty days of the service of the notice.
- (3) If the employer is of opinion that he is not liable to deposit compensation, he shall in his statement indicate the grounds on which he disclaims liability.
- (4) Where the employer has so disclaimed liability, the Commissioner, after such enquiry as he may think fit, may inform any of the dependants of the deceased workman that it is open to the dependants to prefer a claim for compensation, and may give them such other further information as he may think fit.

REPORTS OF FATAL ACCIDENTS AND SERIOUS BODILY INJURIES (Sec 10B)

- (1) Where, by any law for the time being in force, notice is required to be given to any authority, by or on behalf of an employer, of any accident occurring on his premises which results in death, or serious bodily injury, the person required to give the notice shall, within seven days of the death or serious bodily injury, send a report to the Commissioner giving the circumstances attending the death or serious bodily injury: Provided that where the State Government has so prescribed the person required to give the notice may instead of sending such report to the Commissioner send it to the authority to whom he is required to give the notice.

Explanation : "Serious bodily injury" means an injury which involves, or in all probability will involve, the permanent loss of the use of, or permanent injury to, any limb, or the permanent loss of or injury to the sight or hearing, or the fracture of any limb, or the enforced absence of the injured person from work for a period exceeding twenty days.

- (2) The State Government may, by notification in the Official Gazette, extend the provisions of sub-section (1) to any class of premises other than those coming within the scope of that sub-section, and may, by such notification, specify the persons who shall send the report to the Commissioner.
- (3) Nothing in this section shall apply to factories to which the Employees' State Insurance Act, 1948 (34 of 1948), applies.

MEDICAL EXAMINATION (Sec 11)

- (1) Where a workman has given notice of an accident, he shall, if the employer, before the expiry of three days from the time at which service of the notice has been effected, offers to have him examined free of charge by a qualified medical practitioner, submit himself for such examination, and any workman who is in receipt of a half-monthly payment under this Act shall, if so required, submit himself for such examination from time to time :
Provided that a workman shall not be required to submit himself for examination by a medical practitioner otherwise than in accordance with rules made under this Act, or at more frequent intervals than may be prescribed.
- (2) If a workman, on being required to do so by the employer under sub-section (1) or by the Commissioner at any time, refuses to submit himself for examination by a qualified medical practitioner or in any way obstructs the same, his right to compensation shall be suspended during the continuance of such refusal or obstruction unless, in the case of refusal, he was prevented by any sufficient cause from so submitting himself.



- (3) If a workman, before the expiry of the period within which he is liable under sub-section (1) to be required to submit himself for medical examination, voluntarily leaves without having been so examined the vicinity of the place in which he was employed, his right to compensation shall be suspended until he returns and offers himself for such examination.
- (4) Where a workman, whose right to compensation has been suspended under sub-section (2) or sub-section (3), dies without having submitted himself for medical examination as required by either of those sub-sections, the Commissioner may, if he thinks fit, direct the payment of compensation to the dependants of the deceased workman.
- (5) Where under sub-section (2) or sub-section (3) a right to compensation is suspended, no compensation shall be payable in respect of the period of suspension, and, if the period of suspension commences before the expiry of the waiting period referred to in clause (d) of sub-section (1) of section 4, the waiting period shall be increased by the period during which the suspension continues.
- (6) Where an injured workman has refused to be attended by a qualified medical practitioner whose services have been offered to him by the employer free of charge or having accepted such offer has deliberately disregarded the instructions of such medical practitioner, then if it is proved that the workman has not thereafter been regularly attended by a qualified medical practitioner or having been so attended has deliberately failed to follow his instructions and that such refusal, disregard or failure was unreasonable in the circumstances of the case and that the injury has been aggravated thereby, the injury and resulting disablement shall be deemed to be of the same nature and duration as they might reasonably have been expected to be if the workman had been regularly attended by a qualified medical practitioner, whose instructions he had followed, and compensation, if any, shall be payable accordingly.

CONTRACTING (Sec 12)

- (1) Where any person (hereinafter in this section referred to as the principal) in the course of or for the purposes of his trade or business contracts with any other person (hereinafter in this section referred to as the contractor) for the execution by or under the contractor of the whole or any part of any work which is ordinarily part of the trade or business of the principal, the principal shall be liable to pay to any workman employed in the execution of the work any compensation which he would have been liable to pay if that workman had been immediately employed by him; and where compensation is claimed from the principal, this Act shall apply as if references to the principal were substituted for references to the employer except that the amount of compensation shall be calculated with reference to the wages of the workman under the employer by whom he is immediately employed.
- (2) Where the principal is liable to pay compensation under this section, he shall be entitled to be indemnified by the contractor, or any other person from whom the workman could have recovered compensation and where a contractor who is himself a principal is liable to pay compensation or to indemnify a principal under this section he shall be entitled to be indemnified by any person standing to him in the relation of a contractor from whom the workman could have recovered compensation, and all questions as to the right to and the amount of any such indemnity shall, in default of agreement, be settled by the Commissioner.
- (3) Nothing in this section shall be construed as preventing a workman from recovering compensation from the contractor instead of the principal.
- (4) This section shall not apply in any case where the accident occurred elsewhere than on, in or about the premises on which the principal has undertaken or usually undertakes, as the case may be, to execute the work or which are otherwise under his control or management.

REMEDIES OF EMPLOYER AGAINST STRANGER (Sec 13)

Where a workman has recovered compensation in respect of any injury caused under circumstances creating a legal liability of some person other than the person by whom the compensation was paid to pay damages in respect thereof, the person by whom the compensation was paid and any person who has been called on to pay an indemnity under section 12 shall be entitled to be indemnified by the person so liable to pay damages as aforesaid.

INSOLVENCY OF EMPLOYER (Sec 14)

- (1) Where any employer has entered into a contract with any insurers in respect of any liability under this Act to any workman, then in the event of the employer becoming insolvent or making a composition or



scheme of arrangement with his creditors or, if the employer is a company, in the event of the company having commenced to be wound up, the rights of the employer against the insurers as respects that liability shall, notwithstanding anything in any law for the time being in force relating to insolvency or the winding up of companies, be transferred to and vest in the workman, and upon any such transfer the insurers shall have the same rights and remedies and be subject to the same liabilities as if they were the employer, so, however, that the insurers shall not be under any greater liability to the workman than they would have been under to the employer.

- (2) If the liability of the insurers to the workman is less than the liability of the employer to the workman, the workman may prove for the balance in the insolvency proceedings or liquidation.
- (3) Where in any case such as is referred to in sub-section (1) the contract of the employer with the insurers is void or voidable by reason of non-compliance on the part of the employer with any terms or conditions of the contract (other than a stipulation for the payment of premia), the provisions of that sub-section shall apply as if the contract were not void or voidable, and the insurers shall be entitled to prove in the insolvency proceedings or liquidation for the amount paid to the workman :

Provided that the provisions of this sub-section shall not apply in any case in which the workman fails to give notice to the insurers of the happening of the accident and of any resulting disablement as soon as practicable after he becomes aware of the institution of the insolvency or liquidation proceedings.

- (4) There shall be deemed to be included among the debts which under section 49 of the Presidency-towns Insolvency Act, 1909 (3 of 1909), or under section 61 of the Provincial Insolvency Act, 1920 (5 of 1920), or under section 530 of the Companies Act, 1956 (1 of 1956), are in the distribution of the property of an insolvent or in the distribution of the assets of a company being wound up to be paid in priority to all other debts, the amount due in respect of any compensation the liability wherefore accrued before the date of the order of adjudication of the insolvent or the date of the commencement of the winding up, as the case may be, and those Acts shall have effect accordingly.
- (5) Where the compensation is a half-monthly payment, the amount due in respect thereof shall, for the purposes of this section, be taken to be the amount of the lump sum for which the half-monthly payment could, if redeemable, be redeemed if application were made for that purpose under section 7, and a certificate of the Commissioner as to the amount of such sum shall be conclusive proof thereof.
- (6) The provisions of sub-section (4) shall apply in the case of any amount for which an insurer is entitled to prove under sub-section (3), but otherwise those provisions shall not apply where the insolvent or the company being wound up has entered into such a contract with insurers as is referred to in sub-section (1).
- (7) This section shall not apply where a company is wound up voluntarily merely for to purposes of reconstruction or of amalgamation with another company.

COMPENSATION TO BE FIRST CHARGE ON ASSETS TRANSFERRED BY EMPLOYER (Sec 14A)

Where an employer transfers his assets before any amount due in respect of any compensation, the liability whereof accrued before the date of the transfer has been paid, such amount shall, notwithstanding anything contained in any other law for the time being in force, be a first charge on that part of the assets so transferred as consists of immovable property.

SPECIAL PROVISIONS RELATING TO MASTERS AND SEAMEN (Sec 15)

This Act shall apply in the case of workmen who are masters of ships or seamen subject to the following modifications, namely :

- (1) The notice of the accident and the claim for compensation may, except where the person injured is the master of the ship, be served on the master of the ship as if he were the employer, but where the accident happened and the disablement commenced on board the ship, it shall not be necessary for any seaman to give any notice of the accident.
- (2) In the case of the death of a master or seaman, the claim for compensation shall be made within one year after the news of the death has been received by the claimant or, where the ship has been or is deemed to have been lost with all hands, within eighteen months of the date on which the ship was, or is deemed to have been, so lost.

Provided that the Commissioner may entertain any claim to compensation in any case notwithstanding that the claim has not been preferred in due time as provided in this sub-section, if he is satisfied that the failure so to prefer the claim was due to sufficient cause.



- (3) Where an injured master or seaman is discharged or left behind in any part of India or in any foreign country any depositions taken by any Judge or Magistrate in that part or by any Consular Officer in the foreign country and transmitted by the person by whom they are taken to the Central Government or any State Government shall, in any proceedings for enforcing the claim, be admissible in evidence :
- (a) if the deposition is authenticated by the signature of the Judge, ' Magistrate or Consular Officer before whom it is made;
 - (b) if the defendant or the person accused, as the case may be, had an opportunity by himself or his agent to cross-examine the witness; and
 - (c) if the deposition was made in the course of a criminal proceeding, on proof that the deposition was made in the presence of the person accused; and it shall not be necessary in any case to prove the signature or official character of the person appearing to have signed any such deposition and a certificate by such person that the defendant or the person accused had an opportunity of cross-examining the witness and that the deposition if made in a criminal proceeding was made in the presence of the person accused shall, unless the contrary is proved, be sufficient evidence that he had that opportunity and that it was so made.
- (4) No half-monthly payment shall be payable in respect of the period during which the owner of the ship is, under any law in force for the time being relating to merchant shipping, liable to defray the expenses of maintenance of the injured master or seaman.
- (5) No compensation shall be payable under this Act in respect of any injury in respect of which provision is made for payment of a gratuity, allowance or pension under the War Pensions and Detention Allowances (Mercantile Marine, etc.) Scheme, 1939, or the War Pensions and Detention Allowances (Indian Seamen, etc.) Scheme, 1941, made under the Pensions (Navy, Army, Air Force and Mercantile Marine) Act, 1939, or under War pensions and Detention Allowances (Indian Seaman) Scheme, 1942, made by the Central Government.
- (6) Failure to give a notice or make a claim or commence proceedings within the time required by this Act shall not be a bar to the maintenance of proceedings under this Act in respect of any personal injury, if—
- (a) an application has been made for payment in respect of the injury under any of the schemes referred to in the preceding clause, and
 - (b) the State Government certifies that the said application was made in the reasonable belief that the injury was one in respect of which the scheme under which the application was made makes provision for payments, and that the application was rejected or that payments made in pursuance of the application were discontinued on the ground that the injury was not such an injury, and
 - (c) the proceedings under this Act are commenced within one month from the date on which the said certificate of the State Government was furnished to the person commencing the proceedings.

**SPECIAL PROVISIONS RELATING TO CAPTAINS AND OTHER MEMBERS OF CREW OF AIRCRAFT'S
(Sec 15A)**

This Act shall apply in the case of workmen who are captains or other members of the crew of aircraft's subject to the following modifications, namely :—

- (1) The notice of the accident and the claim for compensation may, except where the person injured is the captain of the aircraft, be served on the captain of the aircraft as if he were the employer, but where the accident happened and the disablement commenced on board the aircraft it shall not be necessary for any member of the crew to give notice of the accident.
- (2) In the case of the death of the captain or other member of the crew, the claim for compensation shall be made within one year after the news of the death has been received by the claimant or, where the aircraft has been or is deemed to have been lost with all hands, within eighteen months of the date on which the aircraft was, or is deemed to have been, so lost :

Provided that the Commissioner may entertain any claim for compensation in any case notwithstanding that the claim has not been preferred in due time as provided in this sub-section, if he is satisfied that the failure so to prefer the claim was due to sufficient cause.

- (3) Where an injured captain or other member of the crew of the aircraft is discharged or left behind in any part of India or in any other country, any depositions taken by any Judge or Magistrate in that part or by



any Consular Officer in the foreign country and transmitted by the person by whom they are taken to the Central Government or any State Government shall, in any proceedings for enforcing the claims, be admissible in evidence—

- (a) if the deposition is authenticated by the signature of the Judge, Magistrate or Consular Officer before whom it is made;
- (b) if the defendant or the person accused, as the case may be, had an opportunity by himself or his agent to cross-examine the witness;
- (c) if the deposition was made in the course of a criminal proceeding, on proof that the deposition was made in the presence of the person accused, and it shall not be necessary in any case to prove the signature or official character of the person appearing to have signed any such deposition and a certificate by such person that the defendant or the person accused had an opportunity of cross-examining the witness and that the deposition if made in a criminal proceeding was made in the presence of the person accused shall, unless the contrary is proved, be sufficient evidence that he had that opportunity and that it was so made.

SPECIAL PROVISIONS RELATING TO WORKMEN ABROAD OF COMPANIES AND MOTOR VEHICLES (Sec 15B)

This Act shall apply—

- (i) in the case of workmen who are persons recruited by companies registered in India and working as such abroad, and
- (ii) persons sent for work abroad along with motor vehicles registered under the Motor Vehicles Act (9 of 1988) as drivers, helpers, mechanics, cleaners or other workmen, subject to the following modifications, namely :
 - (1) The notice of the accident and the claim for compensation may be served on the local agent of the company, or the local agent of the owner of the motor vehicle, in the country of accident, as the case may be,
 - (2) In the case of death of the workman in respect of whom the provisions of this section shall apply, the claim for compensation shall be made within one year after the news of the death has been received by the claimant :

Provided that the Commissioner may entertain any claim for compensation in any case notwithstanding that the claim has not been preferred in due time as provided in this sub-section, if he is satisfied that the failure so to prefer the claim was due to sufficient cause.

- (3) Where an injured workman is discharged or left behind in any part of India or in any other country any depositions taken by any Judge or Magistrate in that part or by any Consular Officer in the foreign country and transmitted by the person by whom they are taken to the Central Government or any State Government shall, in any proceedings for enforcing the claims, be admissible in evidence—
 - (a) If the deposition is authenticated by the signature of the Judge, Magistrate or Consular Officer before whom it is made;
 - (b) If the defendant or the person accused, as the case may be, had an opportunity by himself or his agent to cross-examine the witness;
 - (c) If the deposition was made in the course of a criminal proceeding, on proof that the deposition was made in the presence of the person accused, and it shall not be necessary in any case to prove the signature or official character of the person appearing to have signed any such deposition and a certificate by such person that the defendant or the person accused had an opportunity of cross-examining the witness and that the deposition if made in a criminal proceeding was made in the presence of the person accused shall, unless the contrary is proved, be sufficient evidence that he had that opportunity and that it was so made.

RETURNS AS TO COMPENSATION (Sec 16)

The State Government may, by notification in the Official Gazette, direct that every person employing workmen, or that any specified class of such persons, shall send at such time and in such form and to such authority, as may be specified in the notification, a correct return specifying the number of injuries in respect of which



compensation has been paid by the employer during the previous year and the amount of such compensation together with such other particulars as to the compensation as the State Government may direct.

CONTRACTING OUT (Sec 17)

Any contractor agreement whether made before or after the commencement of this Act, whereby a workman relinquishes any right of compensation from the employer for personal injury arising out of or in the course of the employment, shall be null and void in so far as it purports to remove or reduce the liability of any person to pay compensation under this Act.

PENALTIES (Sec 18A)

- (1) Whoever—
 - (a) Fails to maintain a notice-book which he is required to maintain under sub-section (3) of section 10, or
 - (b) Fails to send to the Commissioner a statement which he is required to send under sub-section (1) of section 10A, or
 - (c) Fails to send a report which he is required to send under section 10B, or
 - (d) Fails to make a return which he is required to make under section 16, shall be punishable with fine which may extend to five thousand rupees.
- (2) No prosecution under this section shall be instituted except by or with the previous sanction of a Commissioner, and no Court shall take cognizance of any offence under this section, unless complaint thereof is made within six months of the date on which the alleged commission of the offence came to the knowledge of the Commissioner.

REFERENCE TO COMMISSIONERS (Sec 19)

- (1) If any question arises in any proceedings under this Act as to the liability of any person to pay compensation (including any question as to whether a person injured is or is not a workman) or as to the amount or duration of compensation (including any question as to the nature or extent of disablement), the question shall, in default of agreement, be settled by a Commissioner.
- (2) No Civil Court shall have jurisdiction to settle, decide or deal with any question which is by or under this Act required to be settled, decided or dealt with by a Commissioner or to enforce any liability incurred under this Act.

APPOINTMENT OF COMMISSIONER (Sec 20)

- (1) The State Government may, by notification in the Official Gazette, appoint any person to be a Commissioner for Workmen's Compensation for such area as may be specified in the notification.
- (2) Where more than one Commissioner has been appointed for any area, the State Government may, by general or special order, regulate the distribution of business between them.
- (3) Any Commissioner may, for the purpose of deciding any matter referred to him for decision under this Act, choose one or more persons possessing special knowledge of any matter relevant to the matter under inquiry to assist him in holding the inquiry.
- (4) Every Commissioner shall be deemed to be a public servant within the meaning of the Indian Penal Code (45 of 1860).

VENUE OF PROCEEDINGS AND TRANSFER (Sec 21)

- (1) Where any matter under this Act is to be done by or before a Commissioner, the same shall, subject to the provisions of this Act and to any rules made hereunder, be done by or before the Commissioner for the area in which -
 - (a) The accident took place which resulted in the injury; or
 - (b) The workman or in case of his death, the dependant claiming the compensation ordinarily resides; or
 - (c) The employer has his registered office Provided that no matter shall be processed before or by a Commissioner, other than the Commissioner having jurisdiction over the area in which the accident took place, without his giving notice in the manner prescribed by the Central Government to the Commissioner having jurisdiction over the area and the State Government concerned :



Provided further that, where the workman, being the master of a ship or a seaman or the captain or a member of the crew of an aircraft or a workman in a motor vehicle or a company, meets with the accident outside India any such matter may be done by or before a Commissioner for the area in which the owner or agent of the ship, aircraft or motor vehicle resides or carries on business or the registered office of the company is situate, as the case may be.

- (1A) If a Commissioner, other than the Commissioner with whom any money has been deposited under section 8, proceeds with a matter under this Act, the former may for the proper disposal of the matter call for transfer of any records or money remaining with the latter and on receipt of such a request, he shall comply with the same.
- (2) If a Commissioner is satisfied that any matter arising out of any proceedings pending before him can be more conveniently dealt with by any other Commissioner, whether in the same State or not, he may, subject to rules made under this Act, order such matter to be transferred to such other Commissioner either for report or for disposal, and, if he does so, shall forthwith transmit to such other Commissioner all documents relevant for the decision of such matter and, where the matter is transferred for disposal, shall also transmit in the prescribed manner any money remaining in his hands or invested by him for the benefit of any party to the proceedings :
- Provided that the Commissioner shall not, where any party to the proceedings has appeared before him, make any order of transfer relating to the distribution among dependants of a lump sum without giving such party an opportunity of being heard.
- (3) The Commissioner to whom any matter is so transferred shall, subject to rules made under this Act, inquire there into and, if the matter was transferred for report, return his report thereon or, if the matter was transferred for disposal, continue the proceedings as if they had originally commenced before him.
- (4) On receipt of a report from a Commissioner to whom any matter has been transferred for report under sub-section (2), the Commissioner by whom it was referred shall decide the matter referred in conformity with such report.
- (5) The State Government may transfer any matter from any Commissioner appointed by it to any other Commissioner appointed by it.

FORM OF APPLICATION (Sec 22)

- (1) Where an accident occurs in respect of which liability to pay compensation under this Act arises, a claim for such compensation may, subject to the provisions of this Act, be made before the Commissioner.
- (1A) Subject to the provisions of sub-section (1), no application for the settlement of any matter by a Commissioner, other than an application by a dependant or dependants for compensation shall be made unless and until some question has arisen between the parties in connection therewith which they have been unable to settle by agreement.
- (2) An application to a Commissioner may be made in such form and shall be accompanied by such fee, if any, as may be prescribed, and shall contain, in addition to any particulars which may be prescribed, the following particulars, namely :—
- (a) a concise statement of the circumstances in which the application is made and the relief or order which the applicant claims;
 - (b) in the case of a claim for compensation against an employer, the date of service of notice of the accident on the employer and, if such notice has not been served or has not been served in due time, the reason for such omission;
 - (c) the names and addresses of the parties; and
 - (d) except in the case of an application by dependants for compensation a concise statement of the matters on which agreement has and of those on which agreement has not been come to.
- (3) If the applicant is illiterate or for any other reason is unable to furnish the required information in writing; the application shall, if the applicant so desires, be prepared under the direction of the Commissioner.

POWER OF COMMISSIONER TO REQUIRE FURTHER DEPOSIT IN CASES OF FATAL ACCIDENT (Sec 22A)

- (1) Where any sum has been deposited by an employer as compensation payable in respect of a workman whose injury has resulted in death, and in the opinion of the Commissioner such sum is insufficient, the



Commissioner may, by notice in writing stating his reasons, call upon the employer to show cause why he should not make a further deposit within such time as may be stated in the notice.

- (2) If the employer fails to show cause to the satisfaction of the Commissioner, the Commissioner may make an award determining the total amount payable, and requiring the employer, to deposit the deficiency.

POWERS AND PROCEDURE OF COMMISSIONERS (Sec 23)

The Commissioner shall have all the powers of a Civil Court under the Code of Civil Procedure, 1908 (5 of 1908) for the purpose of taking evidence on oath (which such Commissioner is hereby empowered to impose) and of enforcing the attendance of witnesses and compelling the production of documents and material objects and the Commissioner shall be deemed to be a Civil Court for all the purposes of section 195 and of Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974).

APPEARANCE OF PARTIES (Sec 24)

Any appearance, application or act, required to be made or done by any person before or to a Commissioner (other than an appearance of a party which is required for the purpose of his examination as a witness) may be made or done on behalf of such person by a legal practitioner or by an official of an Insurance Company or registered trade union or by an Inspector appointed under sub-section (1) of section 8 of the Factories Act, 1948 (63 of 1948), or under sub-section (1) of section 5 of the Mines Act, 1952, (35 of 1952), or by any other officer specified by the State Government in this behalf, authorised in writing by such person, or, with the permission of the Commissioner, by any other person so authorised.

METHOD OF RECORDING EVIDENCE (Sec 25)

The Commissioner shall make a brief memorandum of the substance of the evidence of every witness as the examination of the witness proceeds, and such memorandum shall be written and signed by the Commissioner with his own hand and shall form part of the record :

Provided that, if the Commissioner is prevented from making such memorandum, he shall record the reason of his inability to do so and shall cause such memorandum to be made in writing from his dictation and shall sign the same, and such memorandum shall form a part of the record : Provided further that the evidence of any medical witness shall be taken down as nearly as may be word for word.

COSTS (Sec 26)

All costs, incidental to any proceedings before a Commissioner, shall, subject to rules made under this Act, be in the discretion of the Commissioner.

POWER TO SUBMIT CASES (Sec 27)

A Commissioner may, if he thinks fit, submit any question of law for the decision of the High Court and, if he does so, shall decide the question in conformity with such decision.

REGISTRATION OF AGREEMENTS (Sec 28)

- (1) Where the amount of any lump sum payable as compensation has been settled by agreement, whether by way of redemption of a half-monthly payment or otherwise, or where any compensation has been so settled as being payable to a woman or a person under a legal disability a memorandum thereof shall be sent by the employer to the Commissioner, who shall, on being satisfied as to its genuineness, record the memorandum in a register in the prescribed manner :

Provided that—

- (a) No such memorandum shall be recorded before seven days after communication by the Commissioner of notice to the parties concerned;
- (b) Omitted;
- (c) The Commissioner may at any time rectify the register;
- (d) Where it appears to the Commissioner that an agreement as to the payment of a lump sum whether by way of redemption of a half-monthly payment or otherwise, or an agreement as to the amount of compensation payable to a woman or a person under a legal disability ought not to be registered by reason of the inadequacy of the sum or amount, or by reason of the agreement having been obtained by



fraud or undue influence or other improper means, he may refuse to record the memorandum of the agreement and may make such order including an order as to any sum already paid under the agreement, as he thinks just in the circumstances.

- (2) An agreement for the payment of compensation which has been registered under sub-section (1) shall be enforceable under this Act notwithstanding anything contained in the Indian Contract Act, 1872 (9 of 1872), or in any other law for the time being in force.

EFFECT OF FAILURE TO REGISTER AGREEMENT (Sec 29)

Where a memorandum of any agreement, the registration of which is required by section 28, is not sent to the Commissioner as required by that section, the employer shall be liable to pay the full amount of compensation which he is liable to pay under the provisions of this Act, and notwithstanding anything contained in the proviso to sub-section (1) of, section 4, shall not, unless the Commissioner otherwise directs, be entitled to deduct more than half of any amount paid to the workmen by way of compensation whether under the agreement or otherwise.

APPEALS (Sec 30)

- (1) An appeal shall lie to the High Court from the following orders of a Commissioner, namely:—
- (a) An order awarding as compensation a lump sum whether by way of redemption of a half-monthly payment or otherwise or disallowing a claim in full or in part for a lump sum;
 - (aa) An order awarding interest or penalty under section 4A;
 - (b) An order refusing to allow redemption of a half-monthly payment;
 - (c) An order providing for the distribution of compensation among the dependants of a deceased workman, or disallowing any claim of a person alleging himself to be such dependant;
 - (d) An order allowing or disallowing any claim for the amount of an indemnity under the provisions of sub-section (2) of section 12; or
 - (e) An order refusing to register a memorandum of agreement or registering the same or providing for the registration of the same subject to conditions :

Provided that no appeal shall lie against any order unless a substantial question of law is involved in the appeal and, in the case of an order other than an order such as is referred to in clause (b) unless the amount in dispute in the appeal is not less than three hundred rupees :

Provided further that no appeal shall lie in any case in which the parties have agreed to abide by the decision of the Commissioner, or in which the order of the Commissioner gives effect to an agreement come to by the parties.

Provided further that no appeal by an employer under clause (a) shall lie unless the memorandum of appeal is accompanied by a certificate by the Commissioner to the effect that the appellant has deposited with him the amount payable under the order appealed against.

- (2) The period of limitation for an appeal under this section shall be sixty days.
- (3) The provision of section 5 of the Limitation Act, 1963 (36 of 1963) shall be applicable to appeals under, this section.

WITHHOLDING OF CERTAIN PAYMENTS PENDING DECISION OF APPEAL (Sec 30A)

Where an employer makes an appeal under clause (a) of sub-section (1) of section 30, the Commissioner may, and if so directed by the High Court shall, pending the decision of the appeal withhold payment of any sum in deposit with him.

RECOVERY (Sec 31)

The Commissioner may recover as an arrear of land revenue any amount payable by any person under this Act, whether under an agreement for the payment of compensation or otherwise, and the Commissioner shall be deemed to be a public officer within the meaning of section 5 of the Revenue Recovery Act, 1890 (1 of 1890).

**POWER OF THE STATE GOVERNMENT TO MAKE RULES (Sec 32)**

- (1) The State Government may make rules to carry out the purposes of this Act.
- (2) In particular and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:-
 - (a) For prescribing the intervals at which and the conditions subject to which an application for review may be made under section 6 when not accompanied by a medical certificate;
 - (b) For prescribing the intervals at which and the conditions subject to which a workman may be required to submit himself for medical examination under sub-section (1) of section 11;
 - (c) For prescribing the procedure to be followed by Commissioners in the disposal of cases under this Act and by the parties in such cases;
 - (d) For regulating the transfer of matters and cases from one Commissioner to another and the transfer of money in such cases;
 - (e) For prescribing the manner in which money in the hands of a Commissioner may be invested for the benefit of dependants of a deceased workman and for the transfer of money so invested from one Commissioner to another;
 - (f) For the representation in proceedings before Commissioners of parties who are minors or are unable to make an appearance;
 - (g) For prescribing the form and manner in which memoranda of agreements shall be presented and registered;
 - (h) For the withholding by Commissioners, whether in whole or in part of half-monthly payments pending decision on applications for review of the same;
 - (i) For regulating the scales of costs which may be allowed in proceedings under this Act;
 - (j) For prescribing and determining the amount of the fees payable in respect of any proceedings before a Commissioner under this Act;
 - (k) For the maintenance by Commissioners of registers and records of proceedings before them;
 - (l) For prescribing the classes of employers who shall maintain notice-books under sub-section (3) of section 10, and the form of such notice-books;
 - (m) For prescribing the form of statement to be submitted by employers under section 10A;
 - (n) For prescribing the cases in which the report referred to in section 10B may be sent to an authority other than the Commissioner;
 - (o) For prescribing abstracts of this Act and requiring the employers to display notices containing such abstracts;
 - (p) For prescribing the manner in which diseases specified as occupational diseases may be diagnosed;
 - (q) For prescribing the manner in which diseases may be certified for any of the purposes of this Act;
 - (r) for prescribing the manner in which, and the standards by which, incapacity may be assessed.
- (3) Every rule made under this section shall be laid, as soon as may be after it is made, before the State Legislature.

PUBLICATION OF RULES (Sec 34)

- (1) The power to make rules conferred by section 32 shall be subject to the condition of the rules being made after previous publication.
- (2) The date to be specified in accordance with clause (3) of section 23 of the General Clauses Act, 1897 (10 of 1897), as that after which a draft of rules proposed to be made under section 32 will be taken into consideration, shall not be less than three months from the date on which the draft of the proposed rules was published for general information.
- (3) Rules so made shall be published in the Official Gazette and, on such publication, shall have effect as if enacted in this Act.



RULES TO GIVE EFFECT TO ARRANGEMENTS WITH OTHER COUNTRIES FOR THE TRANSFER OF MONEY PAID AS COMPENSATION (Sec 35)

- (1) The Central Government may, by notification in the Official Gazette, make rules for the transfer to any foreign country of money deposited with a Commissioner under this Act which has been awarded to or may be due to, any person residing or about to reside in Such foreign country and for the receipt, distribution and administration in any State of any money deposited under the law relating to workmen's compensation. in any foreign country, which has been awarded to, or may be due to any person residing or about to reside in any State.:

Provided that no sum deposited under this Act in respect of fatal accidents shall be so transferred without the consent of the employer concerned until the Commissioner receiving the sum has passed orders determining its distribution and apportionment under the provisions of sub-sections (4) and (5) of section 8.

- (2) Where money deposited with a Commissioner has been so transferred in accordance with the rules made under this section, the provisions elsewhere contained in this Act regarding distribution by the Commissioner of compensation deposited with him shall cease to apply in respect of any such money.

RULES MADE BY CENTRAL GOVERNMENT TO BE LAID BEFORE PARLIAMENT (Sec 36)

Every rule made under this Act by the Central Government 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.

**3.4 PAYMENT OF WAGES ACT 1936**

An Act to regulate the payment of wages to certain classes of employed persons.

Whereas it is expedient to regulate the payment of wages to certain classes of persons (employed persons);

It is hereby enacted as follows:

1. EXTENT

- (1) This Act may be called the Payment of Wages Act, 1936.
- (2) It extends to the whole of India.
- (3) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint.
- (4) It applies in the first instance to the payment of wages to persons employed in any factory, to persons employed (otherwise than in a factory) upon any railway by a railway administration or either directly or through a sub-contractor by a person fulfilling a contract with a railway administration and to persons employed in an industrial or other establishment specified in sub-clauses (a) to (g) of clause (ii) of section 2.
- (5) The State Government may after giving three months' notice of its intention of so doing, by notification in the Official Gazette extend the provisions of this Act or any of them to the payment of wages to any class of persons employed in any establishment or class of establishments specified by the Central Government or a State Government under sub-clause (h) of clause (ii) of section 2 :

Provided that in relation to any such establishment owned by the Central Government no such notification shall be issued except with the concurrence of that Government.

- (6) Nothing in this Act shall apply to wages payable in respect of a wage-period which over such wage-period average one thousand six hundred rupees a month or more.

2. BASIC CONCEPTS

- (i) "Employed person" includes the legal representative of a deceased employed person;
 - (a) "Employer" includes the legal representative of a deceased employer;
 - (b) "Factory" means a factory as defined in clause (m) of section 2 of the Factories Act, 1948 (63 of 1948) and includes any place to which the provisions of that Act have been applied under sub-section (1) of section 85 thereof;
- (ii) "Industrial or other establishment" means any—
 - (a) Tramway service or motor transport service engaged in carrying passengers or goods or both by road for hire or reward;
 - (aa) Air transport service other than such service belonging to or exclusively employed in the military, naval or air forces of the Union or the Civil Aviation Department of the Government of India;
 - (b) dock wharf or jetty;
 - (c) inland vessel, mechanically propelled;
 - (d) mine, quarry or oil-field;
 - (e) plantation;
 - (f) workshop or other establishment in which articles are produced, adapted or manufactured with a view to their use, transport or sale;
 - (g) establishment in which any work relating to the construction, development or maintenance of buildings, roads, bridges or canals, or relating to operations connected with navigation, irrigation or to the supply of water or relating to the generation, transmission and distribution of electricity or any other form of power is being carried on;
 - (h) any other establishment or class of establishments which the Central Government or a State Government may, having regard to the nature thereof, the need for protection of persons employed therein and other relevant circumstances, specify, by notification in the Official Gazette.



- (iia) “mine” has the meaning assigned to it in clause (j) of sub-section (1) of section 2 of the Mines Act, 1952 (35 of 1952);
- (iii) “plantation” has the meaning assigned to it in clause (f) of section 2 of the Plantations Labour Act, 1951 (69 of 1951);
- (iv) “prescribed” means prescribed by rules made under this Act;
- (v) “railway administration” has the meaning assigned to it in clause (6) of section 3 of the Indian Railways Act, 1890 (9 of 1890); and
- (vi) “wages” means all remuneration (whether by way of salary allowances or otherwise) expressed in terms of money or capable of being so expressed which would, if the terms of employment, express or implied, were fulfilled, be payable to a person employed in respect of his employment, or of work done in such employment and includes—
 - (a) any remuneration payable under any award or settlement between the parties or order of a court;
 - (b) any remuneration to which the person employed is entitled in respect of overtime work or holidays or any leave period;
 - (c) any additional remuneration payable under the terms of employment (whether called a bonus or by any other name);
 - (d) any sum which by reason of the termination of employment of the person employed is payable under any law, contract or instrument which provides for the payment of such sum, whether with or without deductions, but does not provide for the time within which the payment is to be made;
 - (e) any sum to which the person employed is entitled under any scheme framed under any law for the time being in force, but does not include -
- (1) any bonus (whether under a scheme of profit sharing or otherwise) which does not form part of the remuneration payable under the terms of employment or which is not payable under any award or settlement between the parties or order of a court;
- (2) the value of any house-accommodation, or of the supply of light, water, medical attendance or other amenity or of any service excluded from the computation of wages by a general or special order of the State Government;
- (3) any contribution paid by the employer to any pension or provident fund and the interest which may have accrued thereon;
- (4) any travelling allowance or the value of any travelling concession;
- (5) any sum paid to the employed person to defray special expenses entailed on him by the nature of his employment; or
- (6) any gratuity payable on the termination of employment in cases other than those specified in sub-clause (d).

RULES FOR PAYMENT OF WAGES (Sec 3-6)

RESPONSIBILITY FOR PAYMENT OF WAGES (Sec 3)

Every employer shall be responsible for the payment to persons employed by him of all wages required to be paid under this Act :

Provided that in the case of persons employed (otherwise than by a contractor)—

- (a) in factories if a person has been named as the manager of the factory under clause (f) of sub-section (1) of section 7 of the Factories Act, 1948 (63 of 1948) ;
- (b) in industrial or other establishments if there is a person responsible to the employer for the supervision and control of the industrial or other establishments;
- (c) upon railways (otherwise than in factories) if the employer is the railway administration and the railway administration has nominated a person in this behalf for the local area concerned.

The person so named the person so responsible to the employer or the person so nominated as the case may be shall also be responsible for such payment.

**FIXATION OF WAGE-PERIODS (Sec 4)**

- (1) Every person responsible for the payment of wages under section 3 shall fix periods (in this Act referred to as wage-periods) in respect of which such wages shall be payable;
- (2) No wage-period shall exceed one month.

TIME OF PAYMENT OF WAGES (Sec 5)

- (1) The wages of every person employed upon or in—
 - (a) any railway, factory or industrial or other establishment upon or in which less than one thousand persons are employed, shall be paid before the expiry of the seventh day,
 - (b) any other railway, factory or industrial or other establishment shall be paid before the expiry of the tenth day, after the last day of the wage-period in respect of which the wages are payable:
Provided that in the case of persons employed on a dock, wharf or jetty or in a mine, the balance of wages found due on completion of the final tonnage account of the ship or wagons loaded or unloaded, as the case may be, shall be paid before the expiry of the seventh day from the day of such completion.
- (2) Where the employment of any person is terminated by or on behalf of the employer, the wages earned by him shall be paid before the expiry of the second working day from the day on which his employment is terminated :
Provided that where the employment of any person in an establishment is terminated due to the closure of the establishment for any reason other than a weekly or other recognised holiday, the wages earned by him shall be paid before the expiry of the second day from the day on which his employment is so terminated.
- (3) The State Government may, by general or special order, exempt to such extent and subject to such conditions as may be specified in the order the person responsible for the payment of wages to persons employed upon any railway (otherwise than in a factory) or to persons employed as daily-rated workers in the Public Works Department of the Central Government or the State Government from the operation of this section in respect of wages of any such persons or class of such persons :
Provided that in the case of persons employed as daily-rated workers as aforesaid no such order shall be except in consultation with the Central Government.
- (4) Save as otherwise provided in sub-section (2) all payments of wages shall be made on a working day.

WAGES TO BE PAID IN CURRENT COIN OR CURRENCY NOTES (Sec 6)

All wages shall be in current coin or currency notes or in both - wages cannot be paid in kind. Provided that the employer may after obtaining the written authorisation of the employed person pay him the wages either by cheque or by crediting the wages in his bank account.

DEDUCTIONS WHICH MAY BE MADE FROM WAGES (Sec 7)

- (1) Notwithstanding the provisions of sub-section (2) of section 47 of the Indian Railways Act, 1890 (9 of 1890) the wages of an employed person shall be paid to him without deductions of any kind except those authorised by or under this Act.

Explanation I : Every payment made by the employed person to the employer or his agent shall for the purposes of this Act be deemed to be a deduction from wages.

Explanation II : Any loss of wages resulting from the imposition, for good and sufficient cause upon a person employed of any of the following penalties namely :

- (i) the withholding of increment or promotion (including the stoppage of increment at an efficiency bar);
- (ii) the reduction to a lower post or time scale or to a lower stage in a time scale; or
- (iii) suspension;

shall not be deemed to be a deduction from wages in any case where the rules framed by the employer for the imposition of any such penalty are in conformity with the requirements, if any, which may be specified in this behalf by the State Government by notification in the Official Gazette.



- (2) Deductions from the wages of an employed person shall be made only in accordance with the provisions of this Act and may be of the following kinds only namely :
- (a) Fines;
 - (b) Deductions for absence from duty;
 - (c) Deductions for damage to or loss of goods expressly entrusted to the employed person for custody or for loss of money for which he is required to account where such damage or loss is directly attributable to his neglect or default;
 - (d) Deductions for house-accommodation supplied by the employer or by Government or any housing board set up under any law for the time being in force (whether the Government or the Board is the employer or not) or any other Authority engaged in the business of subsidising house-accommodation which may be specified in this behalf by the State Government by notification in the Official Gazette;
 - (e) Deductions for such amenities, services supplied by the employer as the State Government or any officer specified by it in this behalf may by general or special order authorise.

Explanation : The word “services” in this clause does not include the supply of tools and raw materials required for the purposes of employment;

- (f) Deductions for recovery of advances of whatever nature (including advances for travelling allowance or conveyance allowance) and the interest due in respect thereof or for adjustment of over-payments of wages;
- (ff) Deductions for recovery of loans made from any fund constituted for the welfare of labour in accordance with the rules approved by the State Government and the interest due in respect thereof;
- (fff) Deductions for recovery of loans granted for house-building or other purposes approved by the State Government and the interest due in respect thereof;
- (g) Deductions of income-tax payable by the employed person; [Sec 7(2)g]
- (h) Deductions required to be made by order of a court or other authority competent to make such order;
- (i) Deductions for subscriptions to and for repayment of advances from any provident fund to which the Provident Funds Act 1952 (19 of 1952) applies or any recognised provident funds as defined in section 58A of the Indian Income Tax Act, 1922 (11 of 1922) or any provident fund approved in this behalf by the State Government during the continuance of such approval;
- (j) Deductions for payments to co-operative societies approved by the State Government or any officer specified by it in this behalf or to a scheme of insurance maintained by the Indian Post Office and
- (k) Deductions made with the written authorisation of the person employed for payment of any premium on his life insurance policy to the Life Insurance Corporation Act of India established under the Life Insurance Corporation 1956 (31 of 1956) or for the purchase of securities of the Government of India or of any State Government or for being deposited in any Post Office Saving Bank in furtherance of any savings scheme of any such government.
- (kk) Deductions made with the written authorisation of the employed person for the payment of his contribution to any fund constituted by the employer or a trade union registered under the Trade Union Act, 1926 (16 of 1926) for the welfare of the employed persons or the members of their families or both and approved by the State Government or any officer specified by it in this behalf during the continuance of such approval;
- (kkk) Deductions made with the written authorisation of the employed person for payment of the fees payable by him for the membership of any trade union registered under the Trade Union Act, 1926 (16 of 1926);
- (l) Deductions for payment of insurance premia on Fidelity Guarantee Bonds;
- (m) Deductions for recovery of losses sustained by a railway administration on account of acceptance by the employed person of counterfeit or base coins or mutilated or forged currency notes;
- (n) Deductions for recovery of losses sustained by a railway administration on account of the failure of the employed person to invoice to bill to collect or to account for the appropriate charges due to that administration whether in respect of fares freight demurrage wharfage and crantage or in respect of sale of food in catering establishments or in respect of sale of commodities in grain shops or otherwise;



- (o) Deductions for recovery of losses sustained by a railway administration on account of any rebates or refunds incorrectly granted by the employed person where such loss is directly attributable to his neglect or default;
- (p) Deductions made with the written authorisation of the employed person for contribution to the Prime Minister's National Relief Fund or to such other Fund as the Central Government may by notification in the Official Gazette specify;
- (q) Deductions for contributions to any insurance scheme framed by the Central Government for the benefit of its employees.

Limit on deductions [Sec 7(3)]

- (3) Notwithstanding anything contained in this Act, the total amount of deductions which may be made under sub-section (2) in any wage-period from the wages of any employed person shall not exceed—
 - (i) in cases where such deductions are wholly or partly made for payments to co-operative societies under clause (j) of sub-section (2) seventy-five per cent of such wages and
 - (ii) in any other case fifty per cent of such wages :

Provided that where the total deductions authorised under sub-section (2) exceed seventy five per cent or as the case may be, fifty per cent of the wages the excess may be recovered in such manner as may be prescribed.
- (4) Nothing contained in this section shall be construed as precluding the employer from recovering from the wages of the employed person or otherwise any amount payable by such person under any law for the time being in force other than the Indian Railways Act, 1890 (9 of 1890).

FINES (Sec 8)

- (1) No fine shall be imposed on any employed person save in respect of such acts and omissions on his part as the employer with the previous approval of the State Government or of the prescribed authority may have specified by notice under sub-section (2).
- (2) A notice specifying such acts and omissions shall be exhibited in the prescribed manner on the premises in which the employment carried on or in the case of persons employed upon a railway (otherwise than in a factory) at the prescribed place or places.
- (3) No fine shall be imposed on any employed person until he has been given an opportunity of showing cause against the fine or otherwise than in accordance with such procedure as may be prescribed for the imposition of fines.
- (4) The total amount of fine which may be imposed in any one wage-period on any employed person shall not exceed an amount equal to three per cent of the wages payable to him in respect of that wage-period.
- (5) No fine shall be imposed on any employed person who is under the age of fifteen years.
- (6) No fine imposed on any employed person shall be recovered from him by installments or after the expiry of sixty days from the day on which it was imposed.
- (7) Every fine shall be deemed to have been imposed on the day of the act or omission in respect of which it was imposed.
- (8) All fines and all realisations thereof shall be recorded in a register to be kept by the person responsible for the payment of wages under section 3, in such form as may be prescribed; and all such realisations shall be applied only to such purposes beneficial to the persons employed in the factory or establishment as are approved by the prescribed authority.

Explanation : When the persons employed upon or in any railway, factory or industrial or other establishment are part only of a staff employed under the same management all such realisations may be credited to a common fund maintained for the staff as a whole provided that the fund shall be applied only to such purposes as are approved by the prescribed authority.

DEDUCTIONS FOR ABSENCE FROM DUTY (Sec 9)

- (1) Deductions may be made under clause (b) of sub-section (2) of section 7 only on account of the absence of an employed person from the place or places where by the terms of his employment , he is required to work such absence being for the whole or any part of the period during which he is so required to work.



- (2) The amount of such deduction shall in no case bear to the wages payable to the employed person in respect of the wage-period for which the deduction is made in a larger proportion than the period for which he was absent bears to the total period within such wage-period during which by the terms of his employments he was required to work :

Provided that subject to any rules made in this behalf by the State Government if ten or more employed persons acting in concert absent themselves without due notice (that is to say without giving the notice which is required under the terms of their contracts of employment) and without reasonable cause such deduction from any such person may include such amount not exceeding his wages for eight days as may by any such terms be due to the employer in lieu of due notice.

Explanation : For the purposes of this section an employed person shall be deemed to be absent from the place where he is required to work if although present in such place he refuses in pursuance of a stay-in strike or for any other cause which is not reasonable in the circumstances to carry out his work.

DEDUCTIONS FOR DAMAGE OR LOSS (Sec 10)

- (1) A deduction under clause (c) or clause (o) of sub-section (2) of section 7 shall not exceed the amount of the damage or loss caused to the employer by the neglect or default of the employed person.
- (1A) A deduction shall not be made under clause (c) or clause (m) or clause (n) or clause (o) of sub-section (2) of section 7 until the employed person has been given an opportunity of showing cause against the deduction or otherwise than in accordance with such procedure as may be prescribed for the making of such deductions.
- (2) All such deductions and all realisations thereof shall be recorded in a register to be kept by the person responsible for the payment of wages under section 3 in such form as may be prescribed.

DEDUCTIONS FOR SERVICES RENDERED (Sec 11)

A deduction under clause (d) or clause (e) of sub-section (2) of section 7 shall not be made from the wages of an employed person, unless the house-accommodation amenity or service has been accepted by him as a term of employment or otherwise and such deduction shall not exceed an amount equivalent to the value of the house-accommodation amenity or service supplied and in the case of deduction under the said clause (e) shall be subject to such conditions as the State Government may impose.

DEDUCTIONS FOR RECOVERY OF ADVANCES (Sec 12)

Deductions under clause (f) of sub-section (2) of section 7 shall be subject to the following conditions namely :

- (a) recovery of an advance of money given before employment began shall be made from the first payment of wages in respect of a complete wage-period, but no recovery shall be made of such advances given for traveling-expenses;
- (aa) recovery of an advance of money given after employment began shall be subject to such conditions as the State Government may impose;
- (b) recovery of advances of wages not already earned shall be subject to any rules made by the State Government regulating the extent to which such advances may be given and the installments by which they may be recovered.

DEDUCTIONS FOR RECOVERY OF LOANS (Sec 12A)

Deductions for recovery of loans granted under clause (fff) of sub-section (2) of section 7 shall be subject to any rules made by the State Government regulating the extent to which such loans may be granted and the rate of interest payable thereon.

DEDUCTIONS FOR PAYMENTS TO CO-OPERATIVE SOCIETIES AND INSURANCE SCHEMES (Sec 13)

Deductions under clause (j) and clause (k) of sub-section (2) of section 7 shall be subject to such conditions as the State Government may impose.

MAINTENANCE OF REGISTERS AND RECORDS (Sec 13A)

- (1) Every employer shall maintain such registers and records giving such particulars of persons employed by him the work performed by them the wages paid to them the deductions made from their wages the receipts given by them and such other particulars and in such form as may be prescribed.



- (2) Every register and record required to be maintained under this section shall for the purposes of this Act be preserved for a period of three years after the date of the last entry made therein.

INSPECTORS (Sec 14)

- (1) An Inspector of Factories appointed under sub-section (1) of section 8 of the Factories Act, 1948 (63 of 1948) shall be an Inspector for the purposes of this Act in respect of all factories within the local limits assigned to him.
- (2) The State Government may appoint Inspectors for the purposes of this Act in respect of all persons employed upon a railway (otherwise than in a factory) to whom this Act applies.
- (3) The State Government may, by notification in the Official Gazette, appoint such other persons as it thinks fit to be Inspectors for the purposes of this Act and may define the local limits within which and the class of factories and industrial or other establishments in respect of which they shall exercise their functions.
- (4) An Inspector may,
- (a) make such examination and inquiry as he thinks fit in order to ascertain whether the provisions of this Act or rules made there under are being observed;
 - (b) with such assistance, if any, as he thinks fit enter inspect and search any premises of any railway factory or industrial or other establishment at any reasonable time for the purpose of carrying out the objects of this Act;
 - (c) supervise the payment of wages to persons employed upon any railway or in any factory or industrial or other establishment;
 - (d) require by a written order the production at such place, as may be prescribed, of any register maintained in pursuance of this Act and taken on the spot or otherwise statements of any persons which he may consider necessary for carrying out the purposes of this Act;
 - (e) seize or take copies of such registers or documents or portions thereof as he may consider relevant in respect of an offence under this Act which he has reason to believe has been committed by an employer;
 - (f) exercise such other powers as may be prescribed :
- Provided that no person shall be compelled under this sub-section to answer any question or make any statement tending to incriminate himself.
- (4A) The provisions of the Code of Criminal Procedure, 1973 (2 of 1974) shall, so far as may be, apply to any search or seizure under this sub-section as they apply to any search or seizure made under the authority of a warrant issued under section 94 of the said Code.
- (5) Every Inspector shall be deemed to be a public servant within the meaning of the Indian Penal Code (45 of 1860).

FACILITIES TO BE AFFORDED TO INSPECTORS (Sec 14A)

Every employer shall afford an Inspector all reasonable facilities for making any entry inspection supervision examination or inquiry under this Act.

CLAIMS ARISING OUT OF DEDUCTIONS FROM WAGES OR DELAY IN PAYMENT OF WAGES AND PENALTY FOR MALICIOUS OR VEXATIOUS CLAIMS (Sec 15)

- (1) The State Government may, by notification in the Official Gazette, appoint a presiding officer of any Labour Court or Industrial Tribunal constituted under the Industrial Disputes Act 1947 (14 of 1947) or under any corresponding law relating to the investigation and settlement of industrial disputes in force in the State or any Commissioner for Workmen's Compensation or other officer with experience as a Judge of a Civil Court or as a Stipendiary Magistrate to be the authority to hear and decide for any specified area all claims arising out of deductions from the wages or delay in payment of the wages of persons employed or paid in that area including all matters incidental to such claims :
- Provided that where the State Government considers it necessary so to do it may appoint more than one authority for any specified area and may by general or special order provide for the distribution or allocation of work to be performed by them under this Act.



- (2) Where contrary to the provisions of this Act any deduction has been made from the wages of an employed person or any payment of wages has been delayed such person himself or any legal practitioner or any official of a registered trade union authorised in writing to act on his behalf or any Inspector under this Act or any other person acting with the permission of the authority appointed under sub-section (1) may apply to such authority for a direction under sub-section (3) :

Provided that every such application shall be presented within twelve months from the date on which the deduction from the wages was made or from the date on which the payment of the wages was due to be made as the case may be :

Provided further that any application may be admitted after the said period of twelve months when the applicant satisfies the authority that he had sufficient cause for not making the application within such period.

- (3) When any application under sub-section (2) is entertained the authority shall hear the applicant and the employer or other person responsible for the payment of wages under section 3, or give them an opportunity of being heard and after such further inquiry (if any), as may be necessary, may without prejudice to any other penalty to which such employer or other person is liable under this Act direct the refund to the employed person of the amount deducted or the payment of the delayed wages together with the payment of such compensation as the authority may think fit not exceeding ten times the amount deducted in the former case and not exceeding twenty-five rupees in the latter and even if the amount deducted or the delayed wages are paid before the disposal of the application direct the payment of such compensation as the authority may think fit not exceeding twenty-five rupees :

Provided that no direction for the payment of compensation shall be made in the case of delayed wages if the authority is satisfied that the delay was due to—

- (a) A bona fide error or bona fide dispute as to the amount payable to the employed person or
 - (b) The occurrence of an emergency or the existence of exceptional circumstances such that the person responsible for the payment of the wages was unable though exercising reasonable diligence to make prompt payment or
 - (c) The failure of the employed person to apply for or accept payment.
- (4) If the Authority hearing an application under this section is satisfied—
- (a) That the application was either malicious or vexatious the authority may direct that a penalty not exceeding fifty rupees be paid to the employer or other person responsible for the payment of wages by the person presenting the application; or
 - (b) That in any case in which compensation is directed to be paid under sub-section (3) the applicant ought not to have been compelled to seek redress under this section the authority may direct that a penalty not exceeding fifty rupees be paid to the State Government by the employer or other person responsible for the payment of wages.
- (4A) Where there is any dispute as to the person or persons being the legal representative or representatives of the employer or of the employed person the decision of the authority on such dispute shall be final.
- (4B) Any inquiry under this section shall be deemed to be a judicial proceeding within the meaning of sections 193 219 and 228 of the Indian Penal Code (45 of 1860).
- (5) Any amount directed to be paid under this section may be recovered—
- (a) If the authority is a Magistrate by the authority as if it were a fine imposed by him as Magistrate and
 - (b) If the authority is not a Magistrate by any Magistrate to whom the authority makes application in this behalf as if it were a fine imposed by such Magistrate.

SINGLE APPLICATION IN RESPECT OF CLAIMS FROM UNPAID GROUP (Sec 16)

- (1) Employed persons are said to belong to the same unpaid group if they are borne on the same establishment, and if deductions have been made from their wages in contravention of this Act for the same cause and during the same wage-period or periods, or if their wages for the same wage-period or periods have remained unpaid after the day fixed by section 5.



- (2) A single application may be presented under section 15 on behalf or in respect of any number of employed persons belonging to the same unpaid group and in such case every person on whose behalf such application is presented may be awarded maximum compensation to the extent specified in sub-section (3) of section 15.
- (3) The Authority may deal with any number of separate pending applications, presented under section 15 in respect of persons belonging to the same unpaid group, as a single application presented under sub-section (2) of this section and the provisions of that sub-section shall apply accordingly.

APPEAL (Sec 17)

- (1) An appeal against an order dismissing either wholly or in part an application made under sub-section (2) of section 15, or against a direction made under sub-section (3) or sub-section (4) of that section, may be preferred within thirty days of the date on which the order or direction was made in a Presidency-town before the Court of Small Causes and elsewhere before the District Court—
 - (a) by the employer or other person responsible for the payment of wages under section 3 if the total sum directed to be paid by way of wages and compensation exceeds three hundred rupees or such direction has the effect of imposing on the employer or the other person a financial liability exceeding one thousand rupees, or
 - (b) by an employed person or any legal practitioner or any official of a registered trade union authorised in writing to act on his behalf or any Inspector under this Act or any other person permitted by the authority to make an application under sub-section (2) of section 15, if the total amount of wages claimed to have been withheld from the employed person exceeds twenty rupees or from the unpaid group to which the employed person belongs or belonged exceeds fifty rupees, or
 - (c) by any person directed to pay a penalty under sub-section (4) of section 15.
- (1A) No appeal under clause (a) of sub-section (1) shall lie unless the memorandum of appeal is accompanied by a certificate by the authority to the effect that the appellant has deposited the amount payable under the direction appealed against.
- (2) Save as provided in sub-section (1) any order dismissing either wholly or in part an application made under sub-section (2) of section 15 or a direction made under sub-section (3) or sub-section (4) of that section shall be final.
- (3) Where an employer prefers an appeal under this section the authority against whose decision the appeal has been preferred may and if so directed by the court referred to in sub-section (1) shall pending the decision of the appeal withhold payment of any sum in deposit with it.
- (4) The court referred to in sub-section (1) may if it thinks fit submit any question of law for the decision of the High Court and if it so does shall decide the question in conformity with such decision.

CONDITIONAL ATTACHMENT OF PROPERTY OF EMPLOYER OR OTHER PERSON RESPONSIBLE FOR PAYMENT OF WAGES (Sec 17A)

- (1) Where at any time after an application has been made under sub-section (2) of section 15 the Authority or where at any time after an appeal has been filed under section 17 by an employed person or any legal practitioner or any official of a registered trade union authorised in writing to act on his behalf or any Inspector under this Act or any other person permitted by the Authority to make an application under sub-section (2) of section 15, the Court referred to in that section is satisfied that the employer or other person responsible for the payment of wages under section 3 is likely to evade payment of any amount that may be directed to be paid under section 15 or section 17, the Authority or the Court as the case may be except in cases where the Authority or Court is of opinion that the ends of justice would be defeated by the delay after giving the employer or other person an opportunity of being heard may direct the attachment of so much of the property of the employer or other person responsible for the payment of wages as is in the opinion of the Authority or Court sufficient to satisfy the amount which may be payable under the direction.
- (2) The provisions of the Code of Civil Procedure, 1908 (5 of 1908) relating to attachment before judgment under that Code shall so far as may be apply to any order for attachment under sub-section (1).



POWERS OF AUTHORITIES APPOINTED UNDER SECTION 15 (Sec 18)

Every Authority appointed under sub-section (1) of section 15, shall have all the powers of a civil court under the Code of Civil Procedure, 1908 (5 of 1908) for the purpose of taking evidence and of enforcing the attendance of witnesses and compelling the production of documents and every such Authority shall be deemed to be a Civil Court for all the purposes of section 195 and of Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974).

POWER TO RECOVER FROM EMPLOYER IN CERTAIN CASES (Sec 19)

[Repealed by Act 53 of 1964]

PENALTY FOR OFFENCES UNDER THE ACT (Sec 20)

- (1) Whoever being responsible for the payment of wages to an employed person contravenes any of the provisions of any of the following sections namely section 5 except sub-section (4) thereof section 7 section 8 except sub-section (8) thereof, section 9 section 10 except sub-section (2) thereof and section 11 to 13 both inclusive shall be punishable with fine which shall not be less than two hundred rupees but which may extend to one thousand rupees.
- (2) Whoever contravenes the provisions of section 4 sub-section (4) of section 5 section 6 sub-section (8) of section 8 sub-section (2) of section 10 or section 25 shall be punishable with fine which may extend to five hundred rupees.
- (3) Whoever being required under this Act to maintain any records or registers or to furnish any information or return—
 - (a) fails to maintain such register or record; or
 - (b) willfully refuses or without lawful excuse neglects to furnish such information or return; or
 - (c) willfully furnishes or causes to be furnished any information or return which he knows to be false; or
 - (d) refuses to answer or willfully gives a false answer to any question necessary for obtaining any information required to be furnished under this Act shall for each such offence be punishable with fine which shall not be less than two hundred rupees but which may extend to one thousand rupees.
- (4) Whoever—
 - (a) willfully obstructs an Inspector in the discharge of his duties under this Act; or
 - (b) refuse or willfully neglects to afford an Inspector any reasonable facility for making any entry, inspection, examination, supervision, or inquiry authorised by or under this Act in relation to any railway, factory or industrial or other establishment; or
 - (c) willfully refuses to produce on the demand of an Inspector any register or other document kept in pursuance of this Act; or
 - (d) prevents or attempts to prevent or does anything which he has any reason to believe is likely to prevent any person from appearing before or being examined by an Inspector acting in pursuance of his duties under this Act;

shall be punishable with fine which shall not be less than two hundred rupees but which may extend to one thousand rupees.

- (5) If any person who has been convicted of any offence punishable under this Act is again guilty of an offence involving contravention of the same provision he shall be punishable on a subsequent conviction with imprisonment for a term which shall not be less than one month but which may extend to six months and with fine which shall not be less than five hundred rupees but which may extend to three thousand rupees.

Provided that for the purpose of this sub-section no cognizance shall be taken of any conviction made more than two years before the date on which the commission of the offence which is being punished came to the knowledge of the Inspector.

- (6) If any person fails or willfully neglects to pay the wages of any employed person by the date fixed by the Authority in this behalf, he shall without prejudice to any other action that may be taken against him be punishable with an additional fine which may extend to one hundred rupees for each day for which such failure or neglect continues

**PROCEDURE IN TRIAL OF OFFENCES (Sec 21)**

- (1) No court shall take cognizance of a complaint against any person for an offence under sub-section (1) of section 20 unless an application in respect of the facts constituting the offence has been presented under section 15 and has been granted wholly or in part and the authority empowered under the latter section or the appellate Court granting such application has sanctioned the making of the complaint.
- (2) Before sanctioning the making of a complaint against any person for an offence under sub-section (1) of section 20 the Authority empowered under section 15 or the Appellate Court as the case may be shall give such person an opportunity of showing cause against the granting of such sanction and the sanction shall not be granted if such person satisfies the Authority or Court that his default was due to –
 - (a) a bona fide error or bona fide dispute as to the amount payable to the employed person or
 - (b) the occurrence of an emergency or the existence of exceptional circumstances such that the person responsible for the payment of the wages was unable though exercising reasonable diligence to make prompt payment or
 - (c) the failure of the employed person to apply for or accept payment.
- (3) No Court shall take cognizance of a contravention of section 4 or of section 6 or of a contravention of any rule made under section 26 except on a complaint made by or with the sanction of an Inspector under this Act.
- (3A) No Court shall take cognizance of any offence punishable under sub-section (3) or sub-section (4) of section 20 except on a complaint made by or with the sanction of an Inspector under this Act.
- (4) In imposing any fine for an offence under sub-section (1) of section 20 the court shall take into consideration the amount of any compensation already awarded against the accused in any proceedings taken under section 15.

BAR OF SUITS (Sec 22)

No Court shall entertain any suit for the recovery of wages or of any deduction from wages in so far as the sum so claimed—

- (a) forms the subject of an application under section 15 which has been presented by the plaintiff and which is pending before the authority appointed under that section or of an appeal under section 17; or
- (b) has formed the subject of a direction under section 15 in favour of the plaintiff; or
- (c) has been adjudged in any proceeding under section 15 not to be owed to the plaintiff; or
- (d) could have been recovered by an application under section 15.

PROTECTION OF ACTION TAKEN IN GOOD FAITH (Sec 22A)

No suit prosecution or other legal proceeding shall lie against the government or any officer of the Government for anything which is in good faith done or intended to be done under this Act.

CONTRACTING OUT (Sec 23)

Any contract or agreement whether made before or after the commencement of this Act whereby an employed person relinquishes any right conferred by this Act shall be null and void in so far as it purports to deprive him of such right.

APPLICATION OF ACT TO RAILWAYS AIR TRANSPORT SERVICES MINES AND OILFIELDS (Sec 24)

The powers by this Act conferred upon the State Government shall, in relation to railways air transport services mines and oilfields be powers of the Central Government.

DISPLAY BY NOTICE OF ABSTRACTS OF THE ACT (Sec 25)

The person responsible for the payment of wages of persons employed in a factory or an industrial or other establishment shall cause to be displayed in such factory or industrial or other establishment a notice containing such abstracts of this Act and of the rules made there under in English and in the language of the majority of the persons employed in the factory, or industrial or other establishment as may be prescribed.



PAYMENT OF UNDISBURSED WAGES IN CASE OF DEATH OF EMPLOYED PERSON (Sec 25A)

- (1) Subject to the other provisions of the Act all amounts payable to an employed person as wages shall if such amounts could not or cannot be paid on account of his death before payment or on account of his whereabouts not being known –
 - (a) Be paid to the person nominated by him in this behalf in accordance with the rules made under this Act; or
 - (b) Where no such nomination has been made or where for any reasons such amounts cannot be paid to the person so nominated be deposited with the prescribed authority who shall deal with the amounts so deposited in such manner as may be prescribed.
- (2) Where in accordance with the provisions of sub-section (1) all amounts payable to an employed person as wages—
 - (a) Are paid by the employer to the person nominated by the employer person; or
 - (b) Are deposited by the employer with the prescribed authority, the employer shall be discharged of his liability to pay those wages

RULE-MAKING POWER (Sec 26)

- (1) The State Government may make rules to regulate the procedure to be followed by the authorities and courts referred to in sections 15 and 17.
- (2) The State Government may, by notification in the Official Gazette make, rules for the purpose of carrying into effect the provisions of this Act.
- (3) In particular and without prejudice to the generality of the foregoing power rules made under sub-section (2) may—
 - (a) require the maintenance of such records registers returns and notice as are necessary for the enforcement of the Act prescribe the form thereof and the particulars to be entered in such registers or records;
 - (b) require the display in a conspicuous place on premises where employment is carried on of notices specifying rates of wages payable to persons employed on such premises;
 - (c) Provide for the regulate inspection of the weights measures and weighing machines used by employers in checking or ascertaining the wages of persons employed by them;
 - (d) prescribe the manner of giving notice of the days on which wages will be paid;\
 - (e) prescribe the Authority competent to approve under sub-section (1) of section 8 acts and omissions in respect of which fines may be imposed;
 - (f) prescribe the procedure for the imposition of fines under section 8 and for making of the deductions referred to in section 10;
 - (g) prescribe the conditions subject to which deductions may be made under the proviso the sub-section (2) of section 9;
 - (h) prescribe the authority competent to approve the purposes on which the proceeds of fines shall be expended;
 - (i) prescribe the extent to which advances may be made and the installments by which they may be recovered with reference to clause (b) of section 12;
 - (ia) prescribe the extent to which loans may be granted and the rate of interest payable thereon with reference to section 12A;
 - (ib) prescribe the powers of Inspectors for the purposes of this Act;
 - (j) regulate the scales of costs which may allowed in proceedings under this Act;
 - (k) prescribe the amount of court-fees payable in respect of any proceedings under this Act
 - (l) prescribe the abstracts to be contained in the notices required by section 25;
 - (la) prescribe the form and manner in which nominations may be made for the purposes of sub-section (1) of section 25A the cancellation or variation of any such nomination or the making of



any fresh nomination in the event of the nominee predeceasing the person making nomination and other matters connected with such nominations;

- (lb) specify the authority with whom amounts required to be deposited under clause (b) of subsection (1) of section 25A shall be deposited and the manner in which such authority shall deal with the amounts deposited with it under that clause;
 - (m) provide for any other matter which is to be or may be prescribed.
- (4) In making any rule under this section the State Government may provide that a contravention of the rule shall be punishable with fine which may extend to two hundred rupees.
 - (5) All rules made under this section shall be subject to the condition of previous publication and the date to be specified under clause (3) of section 23 of the General Clauses Act 1897 (10 of 1897) shall not be less than three months from the date on which the draft of the proposed rules was published.
 - (6) Every rule made by the Central Government under this section 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.



3.5 MINIMUM WAGES ACT, 1948

An act to provide for fixing minimum rate of wages in certain employments.

Where it is expedient to provide for fixing minimum rates of wages in certain employments:

It is hereby enacted as follows:

“The justification for statutory fixation of minimum wages is obvious. Such provisions which exists in more advanced countries are even more necessary in India, where worker’s organisations are yet poorly developed and worker’s bargaining power is consequently poor.” (Gazette of India).

BASIC CONCEPTS

In this Act unless there is anything repugnant in the subject or context—

- (a) “Adolescent” means a person who has completed his fourteenth year of age but has not completed his eighteenth year;
- (aa) “Adult” means a person who has completed his eighteenth year of age;
- (b) “Appropriate government” means –
 - (i) In relation to any scheduled employment carried on by or under the authority of the Central Government or a railway administration, or in relation to a mine, oilfield or major port, or any corporation established by a Central Act, the Central Government and
 - (ii) In relation to any other scheduled employment, the State Government;
- (bb) “Child” means a person who has not completed his fourteenth year of age;
- (c) “Competent authority” means the authority appointed by the appropriate government by notification in its Official Gazette to ascertain from time to time the cost of living index number applicable to the employees employed in the scheduled employments specified in such notification;
- (d) “Cost of living index number” in relation to employees in any scheduled employment in respect of which minimum rates of wages have been fixed means the index number ascertained and declared by the competent authority by notification in the Official Gazette to be the cost of living index number applicable to employee in such employment;
- (e) “Employer” means any person who employs, whether directly or through another person, or whether on behalf of himself or any other person, one or more employees, in any scheduled employment in respect of which minimum rates of wages have been fixed under this Act and includes except in sub-section (3) of section 26 –
 - (i) In a factory where there is carried on any scheduled employment in respect of which minimum rates of wages have been fixed under this Act, any person named under clause (f) of sub-section (1) of section 7 of the Factories Act 1948 (63 of 1948) as manager of the factory;
 - (ii) In any scheduled employment under the control of any government in India in respect of which minimum rates of wages have been fixed under this Act, the person or Authority appointed by such Government for the supervision and control of employees or where no person or authority is so appointed, the head of the department;
 - (iii) In any scheduled employment under any local authority in respect of which minimum rates of wages have been fixed under this Act, the person appointed by such authority for the supervision and control of employees or where no person is so appointed, the chief executive officer of the local Authority;
 - (iv) In any other case where there is carried on any scheduled employment in respect of which minimum rates of wages have been fixed under this Act, any person responsible to the owner for the supervision and control of the employees or for the payment of wages;
- (f) “Prescribed” means prescribed by rules made under this Act;
- (g) “Schedule employment” means an employment specified in the Schedule or any process or branch of work forming part of such employment;
- (h) “Wages” means all remuneration, capable of being expressed in terms of money, which would, if the terms of the contract of employment, express or implied, were fulfilled be payable to a person employed



in respect of his employment or work done in such employment and includes house rent allowance but does not include –

- (i) the value of—
 - (a) any house accommodation, supply of light, water, medical attendance, or
 - (b) any other amenity or any service excluded by general or special order of the appropriate government;
 - (ii) any contribution paid by the employer to any person fund or provident fund or under any scheme of social insurance;
 - (iii) any traveling allowance or the value of any traveling concession;
 - (iv) any sum paid to the person employed to defray special expenses entailed on him by the nature of his employment; or
 - (v) any gratuity payable on discharge;
- (i) “employee” means any person who is employed for hire or reward to do any work, skilled or unskilled, manual or clerical, in a scheduled employment in respect of which minimum rates of wages have been fixed; and includes an out-worker to whom any articles or materials are given out by another person to be made up, cleaned, washed, altered, ornamented, finished, repaired, adapted or otherwise processed for sale for the purposes of the trade or business of that other person where the process is to be carried out either in the home of the out-worker or in some other premises not being premises under the control and management of that other person; and also includes an employee declared to be an employee by the appropriate Government, but does not include any member of the Armed Forces of the Union.

FIXING OF MINIMUM RATES OF WAGES (Sec 3)

The responsibility of fixing minimum wages lies with appropriate govt.

The appropriate government shall in the manner hereinafter provided -

- (a) fix the minimum rates of wages payable to employees employed in an employment specified in Part I or Part II of the Schedule and in an employment added to either Part by notification under section 27 :
Provided that the appropriate government may in respect of employees employed in an employment specified in Part II of the Schedule instead of fixing minimum rates of wages under this clause for the whole State fix such rates for a part of the State or for any specified class or classes of such employment in the whole State or part thereof;
- (b) review at such intervals as it may think fit such intervals not exceeding five years the minimum rates of wages so fixed and revise the minimum rates if necessary :

Provided that where for any reason the appropriate government has not reviewed the minimum rates of wages fixed by it in respect of any scheduled employment within any interval of five years nothing contained in this clause shall be deemed to prevent it from reviewing the minimum rates after the expiry of the said period of five years and revising them if necessary and until they are so revised the minimum rates in force immediately before the expiry of the said period of five years shall continue in force.

MINIMUM NUMBER OF EMPLOYEES [Sec 3(1A)]

Notwithstanding anything contained in sub-section (1) the appropriate government may refrain from fixing minimum rates of wages in respect of any scheduled employment in which there are in the whole State less than one thousand employees engaged in such employment but if at any time the appropriate government comes to a finding after such inquiry as it may make or cause to be made in this behalf that the number of employees in any scheduled employment in respect of which it has refrained from fixing minimum rates of wages has risen to one thousand or more it shall fix minimum rates of wages payable to employees in such employment as soon as may be after such finding.

MINIMUM RATES [Sec 3(2)]

The appropriate government may fix

- (a) A minimum rate of wages for time work (hereinafter referred to as “a minimum time rate”);
- (b) A minimum rates of wages for piece work (hereinafter referred to as “a minimum piece rate”);



- (c) A minimum rate of remuneration to apply in the case of employees employed on piece work for the purpose of securing to such employees a minimum rate of wages on a time work basis (hereinafter referred to as “a guaranteed time rate”);
- (d) A minimum rate (whether a time rate or a piece rate) to apply in substitution for the minimum rate which would otherwise be applicable in respect of overtime work done by employees (hereinafter referred to as “overtime rate”).

Where in respect of an industrial dispute relating to the rates of wages payable to any of the employees employed in a scheduled employment any proceeding is pending before a Tribunal or National Tribunal under the Industrial Disputes Act 1947 (14 of 1947) or before any like authority under any other law for the time being in force or an award made by any Tribunal National Tribunal or such authority is in operation and a notification fixing or revising the minimum rates of wages in respect of the scheduled employment is issued during the pendency of such proceeding or the operation of the award then notwithstanding anything contained in this Act the minimum rates of wages so fixed or so revised shall not apply to those employees during the period in which the proceeding is pending and the award made therein is in operation or as the case may be where the notification is issued during the period of operation of an award during that period; and where such proceeding or award relates to the rates of wages payable to all the employees in the scheduled employment no minimum rates of wages shall be fixed or revised in respect of that employment during the said period.

In fixing or revising minimum rates of wages under this section—

- (a) Different minimum rates of wages may be fixed for—
 - (i) Different scheduled employments;
 - (ii) Different classes of work in the same scheduled employment;
 - (iii) Adults, adolescents, children and apprentices;
 - (iv) different localities;
- (b) minimum rates of wages may be fixed by any one or more of the following wage periods; namely :
 - (i) By the hour
 - (ii) By the day
 - (iii) By the month, or
 - (iv) By such other larger wage-period as may be prescribed; and, where such rates are fixed by the day or by the month the manner of calculating wages for a month, or for a day, as the case may be may be, indicated :

Provided that where any wage-periods have been fixed under section 4 of the Payment of Wages Act, 1936 (4 of 1936) minimum wages shall be fixed in accordance therewith.

MINIMUM RATE OF WAGES (Sec 4)

- (1) Any minimum rate of wages fixed or revised by the appropriate government in respect of scheduled employments under section 3 may consist of –
 - (i) a basic rate of wages and a special allowance at a rate to be adjusted at such intervals and in such manner as the appropriate government may direct to accord as nearly as practicable with the variation in the cost of living index number applicable to such workers (hereinafter referred to as the “cost of living allowance”); or
 - (ii) a basic rate of wages with or without the cost of living allowance, and the cash value of the concessions in respect of supplies of essential commodities at concession rates, where so authorised; or
 - (iii) an all-inclusive rate allowing for the basic rate, the cost of living allowance and the cash value of the concessions, if any.
- (2) The cost of living allowance and the cash value of the concessions in respect of supplies of essential commodities at concession rate shall be computed by the competent authority at such intervals and in accordance with such directions as may be specified or given by the appropriate government.

**PROCEDURE FOR FIXING AND REVISING MINIMUM WAGES (Sec 5)**

- (1) In fixing minimum rates of wages in respect of any scheduled employment for the first time under this Act or in revising minimum rates of wages so fixed the appropriate government shall either—
 - (a) appoint as many committees and sub-committees as it considers necessary to hold enquiries and advise it in respect of such fixation or revision as the case may be, or
 - (b) by notification in the Official Gazette, publish its proposals for the information of persons likely to be affected thereby and specify a date not less than two months from the date of the notification on which the proposals will be taken into consideration.
- (2) After considering the advice of the committee or committee appointed under clause (a) of sub-section (1) or as the case may be, all representations received by it before the date specified in the notification under clause (b) of that sub-section, the appropriate government shall by notification in the Official Gazette, fix or as the case may be revise the minimum rates of wages in respect of each scheduled employment and unless such notification otherwise provides it shall come into force on the expiry of three months from the date of its issue :

Provided that where the appropriate government proposes to revise the minimum rates of wages by the mode specified in clause (b) of sub-section (1) the appropriate government shall consult the Advisory Board also.

ADVISORY COMMITTEES AND SUB-COMMITTEES - REPEALED BY THE MINIMUM WAGES (AMENDMENT) ACT, 1957 (Sec 6)**ADVISORY BOARD (Sec 7)**

For the purpose of co-ordinating work of committees and sub-committees appointed under section 5 and advising the appropriate government generally in the matter of fixing and revising minimum rates of wages, the Appropriate Government shall appoint an Advisory Board.

U/s 8 Central Advisory Board—

- (1) For the purpose of advising the Central and State Governments in the matters of the fixation and revision of minimum rates of wages and other matters under this Act, and for co-ordinating the work of the Advisory Boards the Central Government shall appoint a Central Advisory Board.
- (2) The Central Advisory Board shall consist of persons to be nominated by the Central Government representing employers and employees in the scheduled employments, who shall be equal in number, and independent persons not exceeding one-third of its total number of members; one of such independent persons shall be appointed the Chairman of the Board by the Central Government.

U/s 9 Composition of committees etc.—

Each of the committees, sub-committees and the Advisory Board shall consist of persons to be nominated by the appropriate government representing employers and employees in the scheduled employments, who shall be equal in number, and independent persons not exceeding one-third of its total number of members; one of such independent persons shall be appointed the Chairman by the Appropriate Government.

CORRECTION OF ERRORS (Sec 10)

- (1) The appropriate government may at any time by notification in the Official Gazette correct clerical or arithmetical mistakes in any order fixing or revising minimum rates of wages under this Act, or errors arising therein from any accidental slip or omission.
- (2) Every such notification shall as soon as may be after it is issued be placed before the Advisory Board for information.

WAGES IN KIND (Sec 11)

- (1) Minimum wages payable under this Act shall be paid in cash.
- (2) Where it has been the custom to pay wages wholly or partly in kind, the Appropriate Government being of the opinion that it is necessary in the circumstances of the case may by notification in the Official Gazette authorise the payment of minimum wages either wholly or partly in kind.



- (3) If appropriate government is of the opinion that provision should be made for the supply of essential commodities at concession rates the appropriate government may by notification in the Official Gazette authorise the provision of such supplies at concessional rates.
- (4) The cash value of wages in kind and of concessions in respect of supplies of essential commodities at concessional rates authorised under sub-sections (2) and (3) shall be estimated in the prescribed manner.

PAYMENT OF MINIMUM RATE OF WAGES (Sec 12)

- (1) Where in respect of any scheduled employment a notification under section 5 is in force, the employer shall pay to every employee engaged in a scheduled employment under him, wages at a rate not less than the minimum rate of wages fixed by such notification for that class of employees in that employment without any deductions except as may be authorised within such time and subject to such conditions as may be prescribed.
- (2) Nothing contained in this section shall affect the provisions of the Payment of Wages Act, 1936 (4 of 1936).

FIXING HOURS FOR NORMAL WORKING DAY ETC (Sec 13)

- (1) In regard to any scheduled employment minimum rates of wages in respect of which have been fixed under this Act, the Appropriate Government may -
 - (a) Fix the number of hours of work which shall constitute a normal working day, inclusive of one or more specified intervals;
 - (b) Provide for a day of rest in every period of seven days which shall be allowed to all employees or to any specified class of employees and for the payment of remuneration in respect of such days of rest;
 - (c) Provide for payment for work on a day of rest at a rate not less than the overtime rate.
- (2) The provisions of sub-section (1) shall in relation to the following classes of employees apply only to such extent and subject to such conditions as may be prescribed :-
 - (a) Employees engaged on urgent work or in any emergency which could not have been foreseen or prevented;
 - (b) Employees engaged in work in the nature of preparatory or complementary work which must necessarily be carried on outside the limits laid down for the general working in the employment concerned;
 - (c) Employees whose employment is essentially intermittent;
 - (d) Employees engaged in any work which for technical reasons has to be completed before the duty is over;
 - (e) Employees engaged in a work which could not be carried on except at times dependent on the irregular action of natural forces.
- (3) For the purposes of clause (c) of sub-section (2) employment of an employee is essentially intermittent when it is declared to be so by the appropriate government on the ground that the daily hours of duty of the employee or if there be no daily hours of duty as such for the employee the hours of duty normally include periods of inaction during which the employee may be on duty but is not called upon to display either physical activity or sustained attention.

OVERTIME (Sec 14)

- (1) Where an employee, whose minimum rate of wages is fixed under this Act, by the hour by the day or by such a longer wage-period as may be prescribed, works on any day in excess of the number of hours constituting a normal working day, the employer shall pay him for every hour or for part of an hour so worked in excess, at the overtime rate fixed under this Act or under any law of the appropriate government for the time being in force, whichever is higher.
- (2) Nothing in this Act shall prejudice the operation of the provisions of section 59 of the Factories Act, 1948 (63 of 1948) in any case where those provisions are applicable.

**WAGES OF WORKER WHO WORKS FOR LESS THAN NORMAL WORKING DAY (Sec 15)**

If an employee whose minimum rate of wages has been fixed under this Act by the day works on any day on which he was employed for a period less than the requisite number of hours constituting a normal working day he shall save as otherwise hereinafter provided be entitled to receive wages in respect of work done by him on that day as if he had worked for a full normal working day :

Provided however that he shall not be entitled to receive wages for a full normal working day—

- (i) In any case where his failure to work is caused by his unwillingness to work and not by omission of the employer to provide him with work and
- (ii) In such other cases and circumstances as may be prescribed.

WAGES FOR TWO OR MORE CLASSES OF WORK (Sec 16)

Where an employee does two or more classes of work to each of which a different minimum rate of wages is applicable, the employer shall pay to such employee in respect of the time respectively occupied in each such class of work, wages at not less than the minimum rate in force in respect of each such class.

MINIMUM TIME RATE WAGES FOR PIECE WORK (Sec 17)

Where an employee is employed on piece work for which minimum time rate and not a minimum piece rate has been fixed under this Act, the employer shall pay to such employee wages at not less than the minimum time rate.

MAINTENANCE OF REGISTERS AND RECORDS (Sec 18)

- (1) Every employer shall maintain such registers and records giving such particulars of employees employed by him, the work performed by them, the wages paid to them, the receipts given by them and such other particulars and in such form as may be prescribed.
- (2) Every employer shall keep exhibited notices in such manner as may be prescribed in the factory, workshop or place where the employees in the scheduled employment may be employed, or in the case of out-workers in such factory workshop or place as may be used for giving out work to them notices in the prescribed form containing prescribed particulars.
- (3) The appropriate government may, by rules made under this Act, provide for the issue of wage books or wage slips to employees employed in any scheduled employment in respect of which minimum rates of wages have been fixed, and prescribe the manner in which entries shall be made and authenticated in such wage books or wage slips by the employer or his agent.

INSPECTORS (Sec 19)

- (1) The appropriate government may, by notification in the Official Gazette, appoint such persons as it thinks fit to be Inspectors for the purposes of this Act, and define the local limits within which they shall exercise their functions.
- (2) Subject to any rules made in this behalf an Inspector may within the local limits for which he is appointed—
 - (a) enter at all reasonable hours with such assistants (if any) being persons in the service of the government or any local or other public authority as he thinks fit, any premises or place where employees are employed or work is given out to out-workers in any scheduled employment in respect of which minimum rates of wages have been fixed under this Act, for the purpose of examining any register, record of wages or notices required to be kept or exhibited by or under this Act or rules made thereunder, and require the production thereof for inspection;
 - (b) examine any person whom he finds in any such premises or place and who, he has reasonable cause to believe, is an employee employed therein or an employee to whom work is given out therein;
 - (c) require any person giving out-work and any out-workers, to give any information, which is in his power to give, with respect to the names and addresses of the persons to for and from whom the work is given out or received, and with respect to the payments to be made for the work;
 - (d) seize or take copies of such register, record of wages or notices or portions thereof as he may consider relevant in respect of an offence under this Act which he has reason to believe has been committed by an employer; and



- (e) exercise such other powers as may be prescribed.
- (3) Every Inspector shall be deemed to be a public servant within the meaning of the Indian Penal Code, (45 of 1860).
- (4) Any person required to produce any document or thing or to give any information by an Inspector under sub-section (2) shall be deemed to be legally bound to do so within the meaning of section 175 and section 176 of the Indian Penal Code, (45 of 1860).

CLAIMS (Sec 20)

- (1) The appropriate government may by notification in the Official Gazette appoint any Commissioner for Workmen's Compensation or any officer of the Central Government exercising functions as a Labour Commissioner for any region or any officer of the State Government not below the rank of Labour Commissioner or any other officer with experience as a judge for a civil court or as a Stipendiary Magistrate to be the Authority to hear and decide for any specified area all claims arising out of payment of less than the minimum rates of wages, or in respect of the payment of remuneration for days of rest or for work done on such days under clause (b) or clause (c) of sub-section (1) of section 13 or of wages at the overtime rate under section 14 to employees employed or paid in that area.
- (2) Where an employee has any claim of the nature referred to in sub-section (1) the employee himself or any legal practitioner or any official of a registered trade union authorised in writing to act on his behalf or any Inspector or any person acting with the permission of the authority appointed under sub-section (1) may apply to such authority for a direction under sub-section (3) :
Provided that every such application shall be presented within six months from the date on which the minimum wages or other amount became payable :
Provided Further that any application may be admitted after the said period of six months when the applicant satisfies the authority that he had sufficient cause for not making the application within such period.
- (3) When any application under sub-section (2) is entertained the authority shall hear the applicant and the employer or give them an opportunity of being heard, and after such further inquiry, if any, as it may consider necessary may without prejudice to any other penalty to which the employer may be liable under this Act direct —
 - (i) in the case of a claim arising out of payment of less than the minimum rates of wages, the payment to the employee of the amount by which the minimum wages payable to him exceed the amount actually paid, together with the payment of such compensation as the authority may think fit, not exceeding ten times the amount of such excess;
 - (ii) in any other case, the payment of the amount due to the employee, together with the payment of such compensation as the authority may think fit, not exceeding ten rupees; and the authority may direct payment of such compensation in cases where the excess or the amount due is paid by the employer to the employee before the disposal of the application.
- (4) If the authority hearing any application under this section is satisfied that it was either malicious or vexatious it may direct that a penalty not exceeding fifty rupees be paid to be employer by the person presenting the application.
- (5) Any amount directed to be paid under this section may be recovered—
 - (a) if the authority is a Magistrate by the authority as if it were a fine imposed by the authority as a Magistrate or
 - (b) if the authority is not a Magistrate by any Magistrate to whom the authority makes application in this behalf as if it were a fine imposed by such Magistrate.
- (6) Every direction of the authority under this section shall be final.
- (7) Every authority appointed under sub-section (1) shall have all the powers of a civil court under the Code of Civil Procedure, 1908 (5 of 1908) for the purpose of taking evidence and of enforcing the attendance of witnesses and compelling the production of documents and every such authority shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXXV of the Code of Criminal Procedure, 1898 (5 of 1898).

**SINGLE APPLICATION IN RESPECT OF A NUMBER OF EMPLOYEES (Sec 21)**

- (1) Subject to such rules as may be prescribed, a single application may be presented under section 20 on behalf or in respect of any number of employees employed in the scheduled employment in respect of which minimum rates of wages have been fixed, and in such cases the maximum compensation which may be awarded under sub-section (3) of section 20 shall not exceed ten times the aggregate amount of such excess or ten rupees per head, as the case may be.
- (2) The authority may deal with any number of separate pending applications presented under section 20 in respect of employees in the scheduled employments in respect of which minimum rates of wages have been fixed as a single application presented under sub-section (1) of this section and the provisions of that sub-section shall apply accordingly.

PENALTIES FOR CERTAIN OFFENCES (Sec 22)

Any employer who —

- (a) pays to any employee less than the minimum rates of wages fixed for that employee's class of work, or less than the amount due to him under the provisions of this Act, or
- (b) contravenes any rule or order made under section 13; 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 : Provided that in imposing any fine for an offence under this section the court shall take into consideration the amount of any compensation already awarded against the accused in any proceedings taken under section 20.

GENERAL PROVISION FOR PUNISHMENT OF OTHER OFFENCES (Sec 22A)

Any employer who contravenes any provision of this Act or of any rule or order made thereunder shall, if no other penalty is provided for, such contravention by this Act, be punishable with fine which may extend to five hundred rupees.

COGNIZANCE OF OFFENCES (Sec 22B)

- (1) No court shall take cognizance of a complaint against any person for an offence—
 - (a) under clause (a) of section 22 unless an application in respect of the facts constituting such offence has been presented under section 20 and has been granted wholly or in part and the appropriate government or an officer authorised by it in this behalf has sanctioned the making of the complaint;
 - (b) under clause (b) of section 22 or under section 22A except on a complaint made by or with the sanction of an Inspector.
- (2) No court shall take cognizance of an offence—
 - (a) under clause (a) or clause (b) of section 22 unless complaint thereof is made within one month of the grant of sanction under this section;
 - (b) under section 22A unless complaint thereof is made within six months of the date on which the offence is alleged to have been committed.

OFFENCES BY COMPANIES (Sec 22C)

- (1) If the person committing any offence under this Act is 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 :
Provided that nothing contained in this sub-section shall render any such person liable to any punishment provided in this Act 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.
- (2) Notwithstanding anything contained in sub-section (1) where any 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, manager, secretary or other officer of the company, such director, manager, secretary or other officer of the company shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.



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.

PAYMENT OF UNDISBURSED AMOUNTS DUE TO EMPLOYEES (Sec 22D)

All amounts payable by an employer to an employee as the amount of minimum wages of the employee under this Act or otherwise due to the employee under this Act or any rule or order made thereunder shall if such amounts could not or cannot be paid to the employee on account of his death before payment or on account of his whereabouts not being known be deposited with the prescribed authority who shall deal with the money so deposited in such manner as may be prescribed.

PROTECTION AGAINST ATTACHMENT OF ASSETS OF EMPLOYER WITH GOVERNMENT (Sec 22E)

Any amount deposited with the appropriate Government by an employer to secure the due performance of a contract with that Government and any other amount due to such employer from that Government in respect of such contract shall not be liable to attachment under any decree or order of any Court in respect of any debt or liability incurred by the employer other than any debt or liability incurred by the employer towards any employee employed in connection with the contract aforesaid.

APPLICATION OF PAYMENT OF WAGES ACT 1936 TO SCHEDULED EMPLOYMENTS (Sec 22F)

- (1) Notwithstanding anything contained in the Payment of Wages Act 1936 (4 of 1936) the appropriate Government may, by notification in the Official Gazette direct that subject to the provisions of sub-section (2), all or any of the provisions of the said Act shall with such modifications, if any, as may be specified in the notification apply to wages payable to employees in such scheduled employments as may be specified in the notification.
- (2) Where all or any of the provisions of the said Act are applied to wages payable to employees in any scheduled employment under sub-section (1), the Inspector appointed under this Act shall be deemed to be the Inspector for the purpose of enforcement of the provisions so applied within the local limits of his jurisdiction.

EXEMPTION OF EMPLOYER FROM LIABILITY IN CERTAIN CASES (Sec 23)

Where an employer is charged with an offence against this Act, he shall be entitled upon complaint duly made by him to have any other person whom he charges as the actual offender brought before the court at the time appointed for hearing the charge; and if after the commission of the offence has been proved the employer proves to the satisfaction of the court—

- (a) That he has used due diligence to enforce the execution of this Act and
- (b) That the said other person committed the offence in question without his knowledge consent or connivance.

That other person shall be convicted of the offence and shall be liable to the like punishment as if he were the employer and the employer shall be discharged :

Provided that in seeking to prove as aforesaid the employer may be examined on oath and the evidence of the employer or his witness if any shall be subject to cross-examination by or on behalf of the person whom the employer charges as the actual offender and by the prosecution.

BAR OF SUITS (Sec 24)

No court shall entertain any suit for the recovery of wages in so far as the sum so claimed—

- (a) forms the subject of an application under section 20 which has been presented by or on behalf of the plaintiff, or
- (b) Has formed the subject of a direction under that section in favour of the plaintiff, or
- (c) Has been adjudged in any proceeding under that section not to be due to the plaintiff, or
- (d) Could have been recovered by an application under that section.

**CONTRACTING OUT (Sec 25)**

Any contract or agreement, whether made before or after the commencement of this Act, whereby an employee either relinquishes or reduces his right to a minimum rate of wages or any privilege or concession accruing to him under this Act shall be null and void in so far as it purports to reduce the minimum rate of wages fixed under this Act.

EXEMPTION AND EXCEPTIONS (Sec 26)

- (1) The appropriate Government may subject to such conditions if any as it may think fit to impose direct that the provisions of this Act shall not apply in relation to the wages payable to disabled employees.
- (2) The appropriate Government if for special reasons it thinks so fit, by notification in the Official Gazette, direct that subject to such conditions and for such period as it may specify the provisions of this Act or any of them shall not apply to all or any class of employees employed in any scheduled employment or to any locality where there is carried on a scheduled employment.
- (2A) The appropriate Government may if it is of opinion that having regard to the terms and conditions of service applicable to any class of employees in a scheduled employment generally or in a scheduled employment in a local area or to any establishment or a part of any establishment in a scheduled employment it is not necessary to fix minimum wages in respect of such employees of that class or in respect of employees in such establishment or such part of any establishment as are in receipt of wages exceeding such limit as may be prescribed in this behalf direct, by notification in the Official Gazette, and subject to such conditions, if any, as it may think fit to impose that the provisions of this Act or any of them shall not apply in relation to such employees.
- (3) Nothing in this Act shall apply to the wages payable by an employer to a member of his family who is living with him and is dependent on him.

Explanation : In this sub-section a member of the employer's family shall be deemed to include his or her spouse or child or parent or brother or sister.

POWER OF STATE GOVERNMENT TO ADD TO SCHEDULE (Sec 27)

The appropriate Government after giving by notification in the Official Gazette not less than three months' notice of its intention so to do may by like notification add to either Part of the Schedule any employment in respect of which it is of opinion that minimum rates of wages should be fixed under this Act and thereupon the Schedule shall in its application to the State be deemed to be amended accordingly.

POWER OF CENTRAL GOVERNMENT TO GIVE DIRECTIONS (Sec 28)

The Central Government may give directions to a State Government as to the carrying into execution of this Act in the State.

POWER OF CENTRAL GOVERNMENT TO MAKE RULES (Sec 29)

The Central Government may, subject to the condition of previous publication, by notification in the Official Gazette, make rules prescribing the term of office of the members, the procedure to be followed in the conduct of business, the method of voting the manner of filling up casual vacancies in membership and the quorum necessary for the transaction of business of the Central Advisory Board.

POWER OF APPROPRIATE GOVERNMENT TO MAKE RULES (Sec 30)

- (1) The appropriate Government may subject to the condition of previous publication, by notification in the Official Gazette, make rules for carrying out the purposes of this Act.
- (2) Without prejudice to the generality of the foregoing power such rules may -
 - (a) Prescribe the term of office of the members the procedure to be followed in the conduct of business the method of voting the manner of filling up casual vacancies in membership and the quorum necessary for the transaction of business of the committees sub-committees and the Advisory Board;
 - (b) Prescribe the method of summoning witnesses production of documents relevant to the subject-matter of the enquiry before the committees, sub-committees and the Advisory Board;



- (c) prescribe the mode of computation of the cash value of wages in kind and of concessions in respect of supplies of essential commodities at concession rates;
- (d) Prescribe the time and conditions of payment of and the deductions permissible from wages;
- (e) Provide for giving adequate publicity to the minimum rates of wages fixed under this Act;
- (f) provide for a day of rest in every period of seven days and for the particulars to be entered in such registers and records;
- (g) Prescribe the number of hours of work which shall constitute a normal working day;
- (h) Prescribe the cases and circumstance in which an employee employed for a period of less than the requisite number of hours constituting a normal working day shall not be entitled to receive wages for a full normal working day;
- (i) Prescribe the form of registers and records to be maintained and the particulars to be entered in such registers and records;
- (j) Provide for the issue of wage book and wage slips and prescribe the manner of making and authenticating entries in wage books and wage slips;
- (k) Prescribe the powers of Inspectors for purposes of this Act;
- (l) Regulate the scale of costs that may be allowed in proceedings under section 20 and
- (m) Prescribe the amount of court-fees payable in respect of proceedings under section 20; and
- (n) Provide for any other matter which is to be or may be prescribed.

RULES MADE BY CENTRAL GOVERNMENT TO BE LAID BEFORE PARLIAMENT (Sec 30A)

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 two successive sessions and if before the expiry of the session in which it is so laid or the session immediately following 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.

VALIDATION OF FIXATION OF CERTAIN MINIMUM RATES OF WAGES (Sec 31)

Where during the period—

- (a) Commencing on the 1st day of April 1952 and ending with the date of the commencement of the Minimum Wages (Amendment) Act 1954 (26 of 1954); or
- (b) Commencing on the 31st day of December 1954 and ending with the date of the commencement of the Minimum Wages (Amendment) Act 1957 (30 of 1957); or
- (c) Commencing on the 31st day of December 1959 and ending with the date of the commencement of the Minimum Wages (Amendment) Act 1961 (31 of 1961) minimum rate of wages have been fixed by an appropriate government as being payable to employees employed in any employment specified in the Schedule in the belief or purported belief that such rates were being fixed under clause (a) of sub-section (1) of section 3 as in force immediately before the commencement of the Minimum Wages (Amendment) Act 1954 (26 of 1954) or the Minimum Wages (Amendment) Act 1957 (30 of 1957) or the Minimum (Amendment) Act 1961 (31 of 1961) as the case may be such rates shall be deemed to have been fixed in accordance with law and shall not be called in question in any court on the ground merely that the relevant date specified for the purpose in that clause had expired at the time the rates were fixed :

Provided that nothing contained in this section shall extend or be construed to extend to affect any person with any punishment or penalty whatsoever by reason of the payment by him by way of wages to any of his employees during any period specified in this section of an amount which is less than the minimum rates of wages referred to in this section or by reason of non-compliance during the period aforesaid with any order or the rule issued under section 13.



3.6 EMPLOYEES' PROVIDENT FUNDS AND MISCELLANEOUS PROVISIONS ACT, 1952

This Act may be called the Employees' Provident Funds and Miscellaneous Provisions Act, 1952

The Employees' Provident Fund & MP Act, 1952 is an important piece of Labour Welfare legislation enacted by the Parliament to provide social security benefits to the workers. At present, the Act and the Schemes framed there under provides for three types of benefits-Contributory Provident Fund, Pensionary benefits to the employees/ family members and the insurance cover to the members of the Provident Fund.

Objective

The Employees Provident fund and Miscellaneous Provisions Act, 1952 is a social security measure, aimed at promoting and securing the well being of the employees by way of provident fund, family pension and insurance to them.

Inculcating a habit of saving amongst workers, providing a steady workforce to the employers and assisting the government by providing funds of considerable magnitude for utilization on various projects meant for promoting economic and social development of the country and the well being of its people.

The object of the Act in 1952 was the institution of the compulsory contributory Provident Fund to the employees to which both the employee and the employer would contribute. The Employees' Provident Fund Scheme was accordingly framed under the Act and it came into effect from 1-11-1952. Initially the title of the Act, was, "The Provident Fund Act, 1952".

On a review of the working of the scheme over the years, it was found that in the event of the premature death of the employees the accumulation in the Provident Fund were too meagre to the family of the deceased. Thus another social security benefit of providing Family Pension through the Employees' Family Pension Fund Scheme, 1971 was introduced by amending the Act. At this stage, the Act was renamed as "The Employees' Provident Fund & Family Pension Act, 1952" and the Employees' Family Pension Scheme came into force on 1-3-1971.

The Act was further amended in the year 1976 to introduce another social security benefit to provide an insurance cover to the members of the Provident Fund in covered establishment. The Employees' Deposit Linked Insurance Scheme, 1976 came into force from 1-8-1976. The name of the Act was then changed to the present one i.e. 'The Employees' Provident Fund & MP Act, 1952'. From 16-11-1995, the Employees' Pension Scheme has come into force which provides pension to retiring employees on reaching 50/58 years of age, widow pension, children pension and nominee pension on death of the member to his eligible family members. This replaces the Employees' Family Pension Scheme, 1971.

The provisions of the Employees' Provident Fund & MP Act, 1952 extends to whole of India except the State of Jammu & Kashmir and also the State of Sikkim where it has not been notified so far after its annexation with the Union of India.

The State Government of Jammu & Kashmir have instituted a separate Provident Fund Scheme w.e.f. 1-6-1961.

Basic Concepts

- (a) Employee [Sec. 2(f)] means any person who—
- (i) is employed
 - for wages
 - in any kind of work, manual or otherwise
 - in or in connection with the work of an establishment, and
 - (ii) gets his wages directly or indirectly from the employer.

Thus 'employee' includes-

- (i) any person employed by or through a contractor in or in connection with the work of an establishment,
- (ii) engaged as an apprentice but not under Apprentices Act, 1961 or under standing order of the establishment.



- (b) Excluded employee means—
- (i) an employee who had been member of the Fund, but withdrew the full accumulated amount in the Fund after his retirement;
 - (ii) an employee who is otherwise eligible, gets monthly salary above ` 6500/-.
- (c) Exempted employee [sec. 2(ff)] means an employee to whom EPF scheme & EDLI scheme would have applied but for the exemption granted u/s 17.
- (d) Exempted establishment [sec.2(fff)] means an establishment in respect of which exemption has been granted u/s 17 from operation of all or any of the provisions of any EPF scheme & EDLI scheme, as the case may be, whether such exemption has been granted to the establishment as such or to any person or class of persons employed therein.
- (e) Basic wages [sec. 2(b)]. The section has defined 'basic wages' in both inclusive and exclusive manner. It includes all emoluments earned by an employee while on duty or on leave/holidays with wages in accordance with terms of contract of employment and paid/payable to him in cash. But the following are excluded from 'basic wages':
- (i) the cash value of any food concession;
 - (ii) any dearness allowance or any other allowance by whatever name it is called paid to the employee on account of rise in cost of living or in respect of work done by him in such employment, for e.g HRA, OT, bonus, commission etc ; and
 - iii) any presents made by the employer.

Applicability

The Act shall apply to every establishment which is a factory engaged in any industry mentioned in Schedule I of the Act and employing 20 or more persons or any other establishment employing twenty or more persons or such other establishment as the central Government may notify.

All employees in such factory or establishment including contract labour, but excluding casual labour and receiving wages up to ` 6,500/- per month will be regulated by the provisions of the Act. Trainee and apprentices not engaged under the Apprentice Act, 1961 are also included in determination of the numerical strength.

Once the Act applies to any establishment, it shall continue to be governed by the Act, irrespective of the fact that the number of employees working therein have subsequently fallen below 20.

The Act initially applied to factories/establishments falling within six specified industries which had completed three years of existence and employed 50 or more persons. With effect from 31-12-1960, the establishments employing 20 or more persons were also brought under the purview of the Act.

Under the infancy protection, the Act was not applicable for the establishment employing 50 or more persons, up to a period of three years from the date of set up. Infancy of five years was allowed in the case of establishment employing twenty or more persons but less than 50 persons.

With effect from 1-8-1988, the Act is applicable to the establishment employing twenty or more persons on expiry of a period of three years from the date of set up. From 22-9-1997 this infancy of three years has been dispensed with and all the establishments employing 20 or more persons are brought under the purview of the Act from the very date of set up subject to fulfillment of other conditions. The provisions of the Act applies on its own force independently.

The Central Government has residual powers to apply this act to any establishment employing less than twenty employees. By virtue of these provisions, the Employees' Provident Fund Scheme has been extended to Cinema theaters employing five or more persons, w.e.f. 1-10-1984. Also there is a provision for voluntary application of the Act to any establishment upon joint request from the employer and majority of its employees, to whom it does not apply otherwise. An establishment to which this Act applies shall continue to be governed by this Act notwithstanding that the number of persons employed therein at any time falls below twenty.

The Act does not apply to certain establishments as specified under Section 16 of the Act.

The Employees' Provident Fund organisation came into being following enactment of the Employees' Provident Fund Act in the year 1952. The funds established under the Act vests in and administered by Central Board of Trustees constituted by Central Government which functions subject to overall regulatory control of the Central Government.

**MEMBERSHIP**

At the inception of the scheme an employee who was in receipt of pay up to ₹ 300/- p.m., and who worked for one year was eligible for membership of the fund. As a result of amendments made from time to time, the conditions of eligibility for membership of the fund have been liberalised in favour of employee. Presently an employee at the time of joining the employment and getting wages upto ₹ 6500/- is required to become a member. Now an employee is eligible for membership of fund from the very first date of joining a covered establishment.

The Act provides for

Grant of exemption from the operation of the scheme/s framed under the Act to an establishment, to a class of employees and to an individual employee, on certain conditions.

- Penalties to employers/trustees of exempted Provident Fund who contravene the provision of the Act and the Scheme.
- Appointment of inspector to secure compliance under the Act and the Schemes framed there under.
- Mode of recovery of moneys due from employers.

1. Provident Fund benefits

1. Employer also contributes to Members PF @ 12% (10% in case of sick industrial co., any establishment having accumulated loss equal to its entire paid up capital and any establishment in Jute Industry, Beedi Industry, Brick Industry, Coir Industry and Gaur Gum Factories.)
2. EPFO guarantees the Employer contribution and credits interest at such rates as determined by the Central Government.
3. Member can withdraw from this accumulations to cater to financial exigencies in life - No need to refund unless misused.
4. On resignation, the member can settle the account. i.e., the member gets his PF contribution, Employer Contribution and Interest.

2. Pension Benefits

1. Pension to Member
2. Pension to Family (on death of member)
3. Scheme Certificate

This Certificate shows the service & family details of a member.

This is issued if the member has not attained the age of 58 while leaving an establishment and he applies for this certificate.

Member can surrender this certificate while joining another establishment and the service stated in the certificate is added with the service he is gaining from the new establishment.

After attaining the age of 50 or above, the member can apply for Pension by surrendering this scheme certificate (if total service is atleast 10 years).

This is a better choice than Withdrawal Benefit, as a member dies holding a valid scheme certificate, his family will get pension (Death when NOT in service).

4. Withdrawal Benefit

If not eligible for pension, member may withdraw the amount accumulated in his pension account.

The calculation of this amount is based only on (i) Last average salary and (ii) Service (Not based on actual amount available in Pension Fund Account)

5. No amount is taken from Member to give Pension to the Member. Employer and Govt. contributes to Pension fund @8.33% and @1.16% respectively
6. EPFO guarantees pension to members, even if the Employer has not contributed to Pension Fund.

3. Death Benefits

1. Provident Fund Amount to Family (or to Nominee);
2. Pension to Family (or to Parent / Nominee);
3. Capital Return of Pension;



4. Insurance (EDLI) amount to Family (or to Nominee).

No amount is taken from Member for this facility. Employer contributes for this.

5. Nominee is basically determined as per the information submitted by the member at this office through FORM-2.

How to become a EPF Member—

You, as your own, can not become an EPF Member. To become an EPF member, you have to work in an establishment which is covered under EPF and MP ACT, 1952.

If 20 or more employees are working in an establishment, EPFO will cover that establishment.

If Employer and Employees of an establishment desires, that establishment can voluntarily opt for EPF coverage even if the employees employed therein is less than 20.

If your establishment is not covered and atleast 20 employees are working in that establishment, you can approach EPFO to cover it.

Contributions

Employees Provident fund scheme takes care of the members at the time of retirement, medical care, housing, family obligations, education of children, finance of insurance policies. etc. In terms of section 6 of the Act, the employee may contribute 12 or 10 %, as the case may be, of the basic wages, dearness allowance including the cash value of any food concession and retaining allowance. An allowance paid to an employee for retaining his services when the establishment is not working is retaining allowance. The rate of contribution shall be 10% in the case of certain establishments.

Any covered establishment with less than 20 employees;

Any sick industrial company with in the meaning of SICA;

Any establishment which has at the end of the financial year accumulated losses equal to or exceeding its entire net worth;

Any establishment in the business of jute, beedi, brick, coir.

If the employee so desires, he may opt to contribute a higher rate also. However, employer does not have to match the voluntary contribution over and above the statutory rate. The employer's contribution of 12% or 10% shall be up to 8.33% of the basic wages, dearness allowance and retaining allowance towards Employees' Pension Scheme and the balance 1.67%/ 3.67% towards the provident fund. The employer's contribution to the Employees deposit linked insurance scheme shall be 0.5 % of the basic wages, dearness allowance, retaining allowance. In addition, the employer has to pay @ 1.10% of 'pay' Contribution and 01% towards administrative charges of fund and insurance scheme respectively. The employee does not have to make any contribution to the pension fund account. These amounts must be paid within 15 days from close of every month with the PF commissioner into the respective accounts maintained with the State bank of India. If the amount is not paid, employer is liable to pay "damages". In addition, criminal prosecution can also be launched.

Filing of returns

The employer shall within 15 days of the applicability of the Act send the particulars of all branches, departments, owners, occupiers, director, partners or any other person in charge of and responsible for the conduct of business, in form 5 A (Return of ownership), in duplicate, to the commissioner. In the event of any change, the same too should be intimated within 15 days to the regional commissioner. The commissioner shall on receipt of the return of ownership verify the particulars submitted therein and after having been satisfied allot an establishment code No. This code shall be mentioned on all forms, challans, statements, returns and all future correspondence.

A return in the prescribed form 5 in respect of employees qualifying to be members of the fund for the first month during the preceding month, shall be filed within 15 days of the close of every month be sent to the CPFC. A monthly return of contributions in the prescribed form 6 has to be filed with the commissioner within 25 days of the close of the month. Annual return of contributions in form 6 A reflecting the employer and employees contribution in respect of each employee is to be submitted within one month of the close of the period of currency to the commissioner.

**Modes of recovery**

The recovery officer shall proceed to recover the amounts in any one or more of the modes given below.

Attachment and sale of moveable or immoveable property of the establishment or employer arrest of the employer and his detention in prison; or

Appointing a receiver for the management of the moveable or immoveable properties of the establishment or employer (Section 8 B).

Offences by Companies

In case of an offence by a company, every person who at the time of the offence was committed was in charge of the company and was responsible for the conduct of business of the company as well as the company itself shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. Unless a person fulfills both the requirements i.e being in charge as well as responsible to the company for the conduct of its business, no prosecution shall lie against him. The words 'deemed' is significant as the company is an artificial person and the person in charge of the company and responsible for the conduct of business bears a vicarious liability for being prosecuted in respect of the offence committed by the company.

However, the person prosecuted can take the defence that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of the offence. if, however, it is proved that the offence was committed with the consent or connivance or is attributable to any neglect on the part of any director, manager, secretary or any other officer of the company then such director, manager, secretary or any other officer shall be deemed to be guilty of that offence and shall be liable to be punished.

Frequently asked questions**- How to withdraw money from EPF**

To withdraw money from EPF Account, you have to either:

Resign or retire from the establishment and apply for settlement of PF in Form-19

- How to get Pension

If you have attained the age of 50 years or more, and

If you have completed a total service of 10 years or more, and

If you are not getting any other EPF Pension.

Then you have to apply in Form-10D at the EPF Office where you last worked through your last employer.

If you want to draw pension from a different place, you have to furnish appropriate Bank / Post Office address in the application form.

Pension is distributed through Post Offices or through some designated banks only (eg: Indian Bank, SBI, Indian Overseas Bank, HDFC Bank, ICICI and UTI Bank).

Four situations when Pension can be applied for :

1. On superannuation Age 58 years or More and atleast ten years of service	The member can continue in service while receiving this pension. On attaining 58 Years of age, a EPF member cease to be a member of EPS automatically.
2. Before superannuation	Age between 50 and 58 years and atleast ten years of service The member should not be in service.
3. Death of the member	Death while in service or Death while not in service.
4. Permanent disability	Permanently and totally unfit for the employment which the member was doing at the time of such disablement.

No pensioner can receive more than one EPF Pension.



-How to settle EPF account

You have to resign or retire from the establishment and apply for settlement of PF in Form-19. If the exit is before 55 years of age, the member should not work in any covered establishment for a period of 2 months from the exit date.

If the member dies, Family members/Nominee have to apply in Form-20 for settlement of PF (In case of death, apply in Form-10D and Form-5IF for Pension and EDLI also)

- How to transfer my account / What to do if I join another establishment

You have to apply in Form-13(R) through the NEW Employer at the EPF Office from which transfer is sought clearly stating New and Old EPF Numbers. You have to obtain new EPF Number from your New Employer. New EPF Number will be allotted by New Employer, not EPFO.

- Employees' Deposit Linked Insurance (EDLI) Scheme

On death of a member, the Family Members or Nominee (whoever has the entitlement to claim Provident Fund amount) can claim for EDLI Benefit. Maximum amount payable is ` 60,000/-. The nominee(s) have to apply in Form-5IF through the Employer. No amount is taken from the Member for this facility. Employer contributes for this. Average PF Balance, salary and service are the factors considered for the calculation of this amount

DO'S FOR A MEMBER

- (1) While joining an establishment, furnish details of previous employment if any, with previous Provident Fund a/c number and scheme certificate.
- (2) In case of existing Provident Fund/ Pension a/c, apply for transfer of previous a/c number to the present a/c number.
- (3) Ensure that employer furnishes Form-5 with details of previous Provident Fund a/c no. to Employees' Provident Fund Organisation.
- (4) Execute Form-2, with details of self, nominee for Provident Fund and pension and details of family, so that it is forwarded to Employees' Provident Fund Organisation by the employer.
- (5) Ensure that particulars furnished are correct in all respects.
- (6) Ensure that enrolment to Employees' Provident Fund/ Employees' Pension Scheme is done immediately on the date of joining the establishment.
- (7) Ensure that Provident Fund is deducted at statutory rate from the total wages i.e. basic, D.A. and retaining allowance if any.
- (8) If desirous of enhancing rate of contribution, inform your willingness with the higher rate opted and forward to Employees' Provident Fund Organisation through employer and allow employer to deduct at enhanced rate from the wages.
- (9) If the wages drawn is more than ` 6500/-, intimate your willingness to contribute on the whole salary as per higher rate to Employees' Provident Fund Organisation through employer. Employer can also contribute on the whole amount drawn as wages under intimation to Employees' Provident Fund Organization.
- (10) Check up periodically with the employer that contribution and other charges are paid to Employees' Provident Fund Organisation and ensure its correctness by verifying the Form-3A (contribution card) maintained by the employer.

DON'TS FOR A MEMBER

- (1) Don't give false declaration and incorrect particulars to Employer and Employees Provident Fund Organisation.
- (2) Don't fall victim to middleman/ agents. Please Contact PRO for Doubts / Clarifications if any.
- (3) Don't allow Employer to deduct his own share of contribution or administrative charges payable by him from your wages.
- (4) Don't be a party to misclassification of allowances of your wages, with a view to avoid payment of Provident Fund.

**3.7 PAYMENT OF BONUS ACT, 1965****INTRODUCTION**

Payment of annual bonus to the employees started in India on the principle of justice and equity to keep the workers happy, as a reward for their performance and also to enable the employers to make profits.

Now it is a well established law after the verdict of the Bombay High Court that the workers could demand bonus as their right and employers should make extra payments for the workers for the work done. (Indian Hume Pipe Vs E.H. Nanavati)

The government of India constituted the Bonus Commission in 1961 and on its recommendation promulgated the Bonus ordinance in 1964 to be replaced by the Bonus Act of 1965.

1. EXTENT

- (1) This Act may be called the Payment of Bonus Act, 1965.
- (2) It extends to the whole of India.

[Note: The words “except the State of Jammu and Kashmir” omitted by Act 51 of 1970, Sec.2 and Schedule (w.e.f. 1st September, 1971).

- (3) Save as otherwise provided in this Act, it shall apply to -
 - (a) Every factory; and
 - (b) Every other establishment in which twenty or more persons are employed on any day during an accounting year.
- (4) Save as otherwise provided in this Act, the provisions of this Act shall in relation to a factory or other establishment to which this Act applies, have effect in respect of the accounting year commencing on any day in the year 1964 and in respect of every subsequent accounting year.

2. The Payment of Bonus Act, 1965 is also referred to as the principal Act.

The Payment of Bonus act was amended in the year 1977 which is as under;

1. SHORT TITLE AND COMMENCEMENT

- (1) This Act may be called the Payment of Bonus (Amendment) Act, 1977.
- (2) It shall come into force on the third day of September, 1977.

2. BASIC CONCEPTS

In this Act, unless the context otherwise requires, -

- (1) “*Accounting year*” means -
 - (i) In relation to a corporation, the year ending on the day on which the books and accounts of the corporation are to be closed and balanced ;
 - (ii) In relation to a company, the period in respect of which any profit and loss account of the company laid before it in annual general meeting is made up, whether that period is a year or not;
 - (iii) In any other case -
 - (a) The year commencing on the 1st day of April; or
 - (b) If the accounts of an establishment maintained by the employer thereof are closed and balanced on any day other than the 31st day of March, then, at the option of the employer, the year ending on the day on which its accounts are so closed and balanced :
Provided that an option once exercised by the employer under para. (b) of this sub-clause shall not again be exercised except with the previous permission in writing of the prescribed authority and upon such conditions as that authority may think fit.
- (2) “Agricultural income” shall have the same meaning as in the Income-tax Act ;
- (3) “Agricultural income-tax law” means any law for the time being in force relating to the levy of tax on agricultural income.



- (4) "Allocable surplus" means -
In relation to an employer, being a company [(Note: Ins. by Act 66 of 1980 (w.e.f. 21st August, 1980) (other than a banking company)] which has not made the arrangements prescribed under the Income-tax Act for the declaration and payment within Indian of the dividends payable out of its profits in accordance with the provisions of Sec.194 of that Act, sixty-seven per cent of the available surplus in an accounting year.
- (5) In any other case, sixty per cent of such available surplus ; (Note: Certain words omitted by Act 23 of 1976, Sec.4 (w.e.f. 25th September, 1975).
- (6) "Available surplus" means the available surplus computed under Sec.5.
- (7) "Award" means an interim or a final determination of any industrial dispute or of any question relating thereto by any Labour Court, Industrial Tribunal or National Tribunal constituted under the Industrial Disputes Act, 1947 (14 of 1947), or by any other authority constituted under any corresponding law relating to investigation and settlement of industrial disputes in force in a State and includes an arbitration award made under Sec. 10-A of that Act or under that law.
- (8) "Banking company" means a banking company as defined in Sec.5 of the Banking Companies Act, 1949 (10 of 1949), and includes the State Bank of India, any subsidiary bank as defined in the State Bank of India (Subsidiary Bank) Act, 1959 (38 of 1959), and any other banking institution which may be notified in this behalf by the Central Government.
- (9) "Company" means any company as defined in Sec.3 of the Companies Act, 1956 (1 of 1956), and includes a foreign company within the meaning of Sec.591 of that Act.
- (10) "Co-operative society" means a society registered or deemed to be registered under the Co-operative Societies Act, 1912 (2 of 1912), or any other law for the time being in force in any State relating to co-operative societies .
- (11) "Corporation" means any body corporate established by or under any Central, Provincial or State Act but does not include a company or a co-operative society .
- (12) "Direct tax" means -
- (a) Any tax chargeable under -
- (i) The Income-tax Act;
 - (ii) The Super Profits Tax Act, 1963 (14 of 1963);
 - (iii) The Companies (Profits) Surtax Act, 1964 (7 of 1964);
 - (iv) The agricultural income-tax law; and
- (b) Any other tax which, having regard to its nature or incidence, may be declared by the Central Government, by notification in the official Gazette to be a direct tax for the purposes of this Act;
- (13) **Employee :** [Sec. 2(13)] means any person (other than an apprentice) employed on salary or wage not exceeding ` 10,000 per month [w.e.f 1.4.2006 by Payment of Bonus (Amendment) Act, 2007] in any industry to do any skilled or unskilled, manual, supervisory, managerial, administrative, technical, or clerical work for hire or reward. It makes no difference whether terms of employment are expressed or implied.
Where the salary or wage of an employee is more than ` 3500/- per mensem, the bonus payable to the employee u/s 10 or u/s 11 shall be calculated as if the salary is ` 3500/- per mensem. This means bonus is payable to employees getting upto ` 10,000 but bonus will be calculated on ` 3500/- only.
- (14) "Employer" includes -
- (i) In relation to an establishment which is factory, the owner or occupier of the factory, including the agent of such owner or occupier, the legal representative of a deceased owner or occupier and where a person has been named as a manager of the factory under Cl. (f) of sub-section (1) of Sec.7 of the Factories Act, 1948, the person named; and
 - (ii) In relation to any other establishment, the person who, or the authority which, has the ultimate control over the affairs of the establishment and where the said affairs are entrusted to a manager, managing director or managing agent, such manager, managing director or managing agent.
- (15) "Establishment in private section" means any establishment other than an establishment in public sector.



- (16) "Establishment in public sector" means an establishment owned, controlled or managed by-
- (a) A Government company as defined in Sec. 617 of the Companies Act, 1956 (1 of 1956) ;
 - (b) A corporation in which not less than forty per cent of its capital is held (whether singly or taken together) by -
 - (i) The Government; or
 - (ii) The Reserve Bank of India; or
 - (iii) A corporation owned by the Government or the Reserve Bank of India.
- (17) "Factory" shall have the same meaning as in Cl. (m) of Sec.2 of the Factories Act, 1948 (63 of 1948).
- (18) "Gross profits" means the gross profits calculated under Sec.4 .
- (19) "Income-tax Act" means the Income-tax Act, 1961 (43 of 1961).
- (20) "Prescribed" means prescribed by rules made under this Act.
- (21) "Salary or wage" means all remuneration (other than remuneration in respect of overtime work) capable of being expressed in terms of money, which would, if the terms of employment, express or implied, were fulfilled, be payable to an employment or of work done in such employment and includes dearness allowance (that is to say, all cash payments, by whatever name called, paid to an employee on account of a rise in the cost of living, but does not include :
 - (i) Any other allowance which the employee is for the time being entitled to ;
 - (ii) The value of any house accommodation or of such of light, water, medical attendance or other amenity or of any service of any confessional supply of food grains or other articles;
 - (iii) Any traveling concession ;
 - (iv) Any bonus (including incentive, production and attendance bonus) ;
 - (v) Any contribution paid or payable by the employer to any pension fund or provident fund or for the benefit of the employees under any law for the time being in force ;
 - (vi) Any retrenchment compensation or any gratuity or other retirement benefit payable to the employees or any ex gratia payment made to him ;
 - (vii) Any commission payable to the employee.
 - (viii) Any commission payable to the employee.
- Explanation** - Where an employee is given in lieu of the whole or part of the salary or wage payable to him, free food allowance or free food by his employer, such food allowance or the value of such food shall, for the purpose of this clause, be deemed to form part of the salary or wage of such employees.
- (22) Words and expressions used but not defined in this Act and defined in the Industrial Disputes Act, 1947 (14 of 1947), shall have the meanings respectively assigned to them in that Act.

3. ESTABLISHMENTS TO INCLUDE DEPARTMENTS, UNDERTAKINGS AND BRANCHES

Where an establishment consists of different departments or undertakings or has branches, whether situated in the same place or in different places, all such departments or undertakings or branches shall be treated as parts of the same establishment for the purpose of computation of bonus under this Act :

Provided that where for any accounting year a separate balance-sheet and profit and loss account are prepared and maintained in respect of any such department or undertaking or branch, then, such department or undertaking or branch shall be treated as separate establishment for the purpose of computation of bonus under this Act for that year, unless such department or undertaking or branch was immediately before the commencement of that accounting year treated as part of the establishment for the purpose of computation of bonus.

NOTES

When there is integral link and unity of management between the two division of a company it cannot be said as a separate undertaking although it is 60 miles away from one division. *Gawlior Rayon Silk Mfg. Co. v. Industrial Tribunal* 1975 Lab. I.C. 820.



COMPUTATION OF GROSS PROFITS (Sec 4)

The gross profits derived by an employer from an establishment in respect of any accounting year shall -

- (a) In the case of a banking company, be calculated in the manner specified in the First Schedule;
- (b) In any other case, be calculated in the manner specified in the Second Schedule.

COMPUTATION OF AVAILABLE SURPLUS (Sec 5)

The available surplus in respect of any accounting year shall be the gross profits for that year after deducting therefrom the sums referred to in Sec.6.

- (a) The gross profits for that accounting year after deducting therefrom the sums referred to in Section 6 ; and
- (b) An amount equal to the difference between -
 - (i) The direct tax, calculated in accordance with the provisions of Section 7, in respect of an amount equal to the gross profits of the employer for the immediately preceding accounting year; and
 - (ii) The direct tax, calculated in accordance with the provisions of Section 7, in respect of an amount equal to the gross profits of the employer for such preceding accounting year after deducting therefrom the amount of bonus which the employer has paid or is liable to pay to his employees in accordance with the provisions of this Act for that year.]

NOTES

The burden of proving that the depreciation claimed is the correct amount admissible under Section 32 (1) of Income-tax Act lies on the party claiming such amount. Workmen of National and Grindlays Bank Ltd. v. National and Grindlays Bank Ltd., AIR 1976 S.C. 611.

SUMS DEDUCTIBLE FROM GROSS PROFITS (Sec 6)

The following sums shall be deducted from the gross profits as prior charges, namely :

- (a) Any amount by way of depreciation admissible in accordance with the provisions of sub-section (1) of Section 32 of the Income-tax Act, or in accordance with the provisions of the agricultural Income-tax law, as the case may be :

Provided that where an employer has been paying bonus of his employees under a settlement or an award or agreement made before the 29th May, 1965, and subsisting on that date after deducting from the gross profits notional normal depreciation, then the amount of depreciation to be deducted under this clause shall, at the option of such employer (such option to be exercised once and within one year from that date) continue to be such notional normal depreciation;
- (b) Any amount by way of development rebate or investment allowance or development allowance] which the employer is entitled to deduction from his income under the Income-tax Act ;
- (c) Subject to the provisions of Section 7, any direct tax which the employer is liable to pay for the accounting year in respect of his income, profits and gains during the year ;
- (d) Such further sums as are specified in respect of the employer in the Act.

CALCULATION OF DIRECT TAX PAYABLE BY THE EMPLOYER (Sec 7)

Any direct tax payable by the employer] for any accounting year shall, subject to the following provisions, be calculated at the rates applicable to the income of the employer for that year, namely :

- (a) In calculating such tax no account shall be taken of—
 - (i) Any loss incurred by the employer in respect of any previous accounting year and carried forward under any law for time being in force relating to direct taxes ;
 - (ii) Any arrears of depreciation which the employer is entitled to add to the amount of the allowance for depreciation for any following accounting year or years under sub-section (2) of Section 32 of the Income-tax Act ;
 - (iii) Any exemption conferred on the employer under Section 84 of the Income-tax Act or of any deduction The Orient Tavern which he is entitled under sub-section (1) of Section 101 of that Act, as in force immediately before the commencement of the Finance Act, 1965 (10 of 1965) ;



- (b) Where the employer is a religious or a charitable institution to which the provisions of Section 32 do not apply and the whole or any part of its income is exempt from tax under the Income-tax Act, then, with respect to the Orient Tavern the income so exempted, such institution shall be treated as if it were a company in which the public are substantially interested within the meaning of that Act ;
- (c) Where the employer is an individual or a Hindu undivided family, the tax payable by such employer under the Income-tax Act shall be calculated on the basis that the income derived by him from the establishment is his only income ;
- (d) Where the income of any employer includes any profits and gains derived from the export of any goods or merchandise out of India any rebate on such income is allowed under any law for the time being in force relating to direct taxes, then, no account shall be taken of such rebate;
- (e) No account shall be taken of any rebate other than development rebate or credit or relief or deduction (not hereinafter mentioned in this section) in the payment of any direct tax allowed under any law for the time being in force relating to direct taxes or under the relevant annual Finance Act, for the development of any industry.

ELIGIBILITY FOR BONUS (Sec 8)

Every employee shall be entitled to be paid by his employer in an accounting year, bonus, in accordance with the provisions of this Act, provided he has worked in the establishment for not less than thirty working days in that year.

DISQUALIFICATION FOR BONUS (Sec 9)

Notwithstanding anything contained in this Act, an employee shall be disqualified from receiving bonus under this Act, if he is dismissed from service for—

- (a) Fraud; or
- (b) Riotous or violent behaviour while on the premises of the establishment; or
- (c) Theft, misappropriation or sabotage of any property of the establishment.

PAYMENT OF MINIMUM BONUS (Sec 10)

Subject to the other provisions of this Act, every employer shall be bound to pay to every employee in respect of the accounting year commencing on any day in the year 1979 and in respect of every subsequent accounting year, a minimum bonus which shall be 8.33 per cent of the salary or wage earned by the employee during the accounting year or one hundred rupees, whichever is higher, whether or not the employer has any allocable surplus in the accounting year :

Provided that there an employee has not employed fifteen years of age at the beginning of the accounting year, the provision of this section shall have effect in relation to such employee as if for the words “one hundred rupees”, the words “sixty rupees” were substituted.

PAYMENT OF MAXIMUM BONUS (Sec 11)

- (1) Where in respect of any accounting year referred to in Sec.10, the allocable surplus exceeds the amount of minimum bonus payable to the employees under that section, the employer shall, in lieu of such minimum bonus, be bound to pay to every employee in respect of that accounting year bonus which shall be an amount in proportion to the salary or wage earned by the employee during the accounting year subject to a maximum of twenty per cent of such salary or wage.
- (2) In computing the allocable surplus under this section, the amount set on or the amount set-off under the provisions of Sec.15 shall be taken into account in accordance with the provisions of that section.

CALCULATION OF BONUS WITH RESPECT TO CERTAIN EMPLOYEES (Sec 12)

Where the salary or wage of an employee exceeds one thousand and six hundred rupees per mensem, the bonus payable to such employee under Sec.10, or as the case may be, under Sec.11, shall be calculated as if his salary or wage were one thousand and six hundred rupees per mensem.



PROPORTIONATE REDUCTION IN BONUS IN CERTAIN CASES (Sec 13)

Where an employee has not worked for all the working days in an accounting year, the minimum bonus of one hundred rupees or, as the case may be, of sixty rupees, if such bonus is higher than 8.33 per cent of his salary or wage for the days he has worked in that accounting year, shall be proportionately reduced.

NOTES

Working days - Words 'working day in any accounting year' - meaning of - factory working in a particular season only and not during the whole year in such a case the 'working days' only mean those days of the year during which the employee concerned is actually allowed to work. (Shakkar Mills Mazdoor Sangh v. Gwalior Sugar Co. Ltd., 1985 111 294 = AIR 1985 SC 758).

COMPUTATION OF NUMBER OF WORKING DAYS (Sec 14)

For the purposes of Sec. 13, an employee shall be deemed to have worked in an establishment in any accounting year also on the days on which—

- (a) He has been laid off under an agreement or as permitted by standing orders under the Industrial Employment (Standing Orders) Act, 1946 (20 of 1946), or under the Industrial Disputes Act, 1947 (14 of 1947) or under any other law applicable to the establishment ;
- (b) He has been on leave with salary or wage ;
- (c) He has been absent due to temporary disablement caused by accident arising out of and in the course of his employment; and
- (d) The employee has been on maternity leave with salary or wage, during the accounting year.

SET-ON AND SET-OFF OF ALLOCABLE SURPLUS (Sec 15)

- (1) Where for any accounting year, the allocable surplus exceeds the amount of maximum bonus payable to the employees in the establishment under Sec.11, the, the excess shall, subject to a limit of twenty per cent of the total salary or wage of the employees employed in the establishment in that accounting year, be carried forward for being set-on in the succeeding accounting year and so on up to and inclusive of the fourth accounting year to be utilized for the purpose of payment of bonus in the manner illustrated in the Fourth Schedule.
- (2) Where for any accounting year, there is no available surplus or the allocable surplus in respect of that year falls short of the amount of minimum bonus payable to the employees in the establishment under Section 10, and there is no amount or sufficient amount carried forward and set on under sub-section (1) which could be utilized for the purpose of payment of the minimum bonus, then, such minimum amount or the deficiency, as the case may be, shall be carried forward for being set-off in the succeeding accounting year and so on up to and inclusive of the fourth accounting year in the manner illustrated in the Fourth Schedule.
- (3) The principle of set-on and set-off as illustrated in the Fourth Schedule shall apply to all other cases not covered by sub-section (1) or sub-section (2) for the purpose of payment of bonus under this Act.
- (4) Where in any accounting year any amount has been carried forward and set-on or set-off under this section, then, in calculating bonus for the succeeding accounting year, the amount of set-on or set-off carried forward from the earliest accounting year shall first be taken into account.

SPECIAL PROVISIONS WITH RESPECT TO CERTAIN ESTABLISHMENTS (Sec 16)

- (1) Where an establishment is newly set up, whether before or after the commencement of this Act, the employees of such establishment shall be entitled to be paid bonus under this Act in accordance with the provisions of sub-section (1-A), (1-B) and (1-C).
- (1-A) In the first five accounting years following the accounting year in which the employee sells the goods produced or manufactured by him or renders services, as the case may be, from such establishment, bonus shall be payable only in respect of the accounting year in which the employer derives profit from such establishment and such bonus shall be calculated in accordance with the provisions of this Act in relation to that year, but without applying the provisions of Sec.15.



(1-B) For the sixth and seventh accounting years following the accounting year in which the employer sells the goods produced or manufactured by him or renders services, as the case may be, from such establishment, the provisions of Sec.15 shall apply subject to the following modifications namely :

(i) For the sixth accounting year -

Set on or set-off, as the case may be, shall be made in the manner illustrated in the [(Note: Subs. by Act 66 of 1980, (w.e.f. 25th September, 1975) Fourth Schedule] taking into account the excess or deficiency, if any, as the case may be, of the allocable surplus set-on or set-off in respect of the fifth and sixth accounting year ;

(ii) For the seventh accounting year -

Set-on or set-off, as the case may be, shall be made in the manner illustrated the [(Note: Subs. by Act 66 of 1980, (w.e.f. 25th September, 1975) Fourth Schedule] taking into account the excess of deficiency, if any, as the case may be, of the allocable surplus set-on or set-off in respect of the fifth, sixth and seventh accounting years.

(1-C) From the eighth accounting year following the accounting year in which the employer sells the goods produced or manufactured by him or renders services, as the case may be, from such establishment, the provisions of Sec.15 shall apply in relation to such establishment as they apply in relation to any other establishment.

Explanation I - For the purpose of sub-section (1), an establishment shall not be deemed to be newly set up merely by reason of a change in its location, management, name or ownership.

Explanation II - For the purpose of sub-section (1-A), an employer shall not be deemed to have derived profit in any accounting year unless -

- (a) He has made provision for that year's depreciation, to which he is entitled under the Income-tax Act or, as the case may be, under the agricultural income-tax law ; and
- (b) The arrears of such depreciation and losses incurred by him in respect of the establishment for the previous accounting years have been fully set-off against his profits.

Explanation III - For the purposes of sub-sections (1-A), (1-B) and (1-C) sale of the goods produced or manufactured during the course of the trial running of any factory or of the prospecting stage or an oil-field shall not be taken into consideration and where any question arises with regard to such production or manufacture, the decision of the appropriate Government, made after giving the parties reasonable opportunity of representing the case, shall be final and shall not be called in question by any Court or other Authority.]

(2) The provisions of [(Note: Subs. by Act 23 of 1976, (w.e.f. 25th September, 1975) sub-sections (1), (1-A), (1-B) and (1-C) shall, so far as may be, apply to new departments or undertakings or branches set up by existing establishments :

Provided that if an employer in relation to an existing establishment consisting of different departments or undertakings or branches (whether or not in the same industry) set up at different periods has, before the 29th May, 1965, been paying bonus to the employees of all such departments or undertakings or branches irrespective of the date on which such departments or undertakings or branches were set up, on the basis of the consolidated profits computed in respect of all such departments or undertakings or branches, then, such employer shall be liable to pay bonus in accordance with the provisions of this Act to the employees of all such departments or undertakings or branches (whether set up before or after that date) on the basis of the consolidated profits computed as aforesaid.

ADJUSTMENT OF CUSTOMARY OR INTERIM BONUS AGAINST BONUS PAYABLE UNDER THE ACT (Sec 17)

Where in any accounting year -

- (a) An employer has paid any puja bonus or other customary bonus to an employees ; or
- (b) An employer has paid a part of the bonus payable under this Act to an employee before the date on which such bonus becomes payable;



Then, the employer shall be entitled to deduct the amount of bonus so paid from the amount of bonus payable by him to the employee under this Act in respect of that accounting year and the employee shall be entitled to receive only the balance.

DEDUCTION OF CERTAIN AMOUNTS FROM BONUS PAYABLE UNDER THE ACT (Sec 18)

Where in any accounting year, an employee is found guilty of misconduct causing financial loss to the employer, then, it shall, be lawful for the employer to deduct the amount of loss from the amount of bonus payable by him to the employee under this Act in respect of that accounting year only and the employee shall be entitled to receive the balance, if any.

TIME-LIMIT FOR PAYMENT OF BONUS (Sec 19)

All amounts payable to an employee by way of bonus under this Act shall be paid in cash by his employer.

(a) Where there is a dispute regarding payment of bonus pending before any authority under Sec.22, within a month from the date on which the award becomes enforceable or the settlement comes into operation, in respect of such dispute;

(b) In any other case, within a period of eight months from the close of the accounting year :

Provided that the appropriate Government or such authority as the appropriate Government may specify in this behalf may, upon an application made to it by the employer and for sufficient reasons, by order, extend the said period of eight months to such further period or periods as it thinks fit ; so, however, that the total period so extended shall not in any case exceed two years.

APPLICATION OF ACT TO ESTABLISHMENTS IN PUBLIC SECTOR IN CERTAIN CASES (Sec 20)

If in any accounting year an establishment in public sector sells any goods produced or manufactured by it or renders any services, in competition with an establishment in private sector, and the income from such sale or services or both is not less than twenty per cent of the gross income of the establishment in public sector for that year, then, the provisions of this Act shall apply in relation to such establishment in public sector as they apply in relation to a like establishment in private sector.

RECOVERY OF BONUS DUE FROM AN EMPLOYER (Sec 21)

Where any money is due to an employee by way of bonus from his employer under a settlement or an award or agreement, the employee himself, or any other person authorised by him in writing in this behalf, or in the case of the death of the employee, his assignee or heirs may, without prejudice to any other mode of recovery made an application to the appropriate Government for the recovery, of the money due to him, and if the appropriate Government or such authority as the appropriate Government may specify in this behalf is satisfied that any money is so due, it shall issue a certificate for that amount to the Collector who shall proceed to recover the same in the same manner as an arrear of land revenue :

Provided that every such application shall be made within one year from the date on which the money became due to the employee from the employer :

Provided further that any such application may be entertained after the expiry of the said period of one year, if the appropriate Government is satisfied that the applicant had sufficient cause for not making the application within the said period.

Explanation - In this section "employee" includes a person who is entitled to the payment of bonus under this Act but who is no longer in employment.

REFERENCE OF DISPUTE UNDER THIS ACT (Sec 22)

Where any dispute arises between an employer and his employees with respect to the bonus payable under this Act or with respect to the application of this Act to an establishment in public sector, then, such dispute shall be deemed to be an industrial dispute within the meaning of the Industrial Dispute Act, 1947 (14 of 1947), or of any corresponding law relating to investigation and settlement of industrial disputes in force in a State and the provisions of that Act or, as the case may be, such law, save as otherwise expressly provided, apply accordingly.

**PRESUMPTION ABOUT ACCURACY OF BALANCE-SHEET AND PROFIT AND LOSS ACCOUNT OF CORPORATIONS AND COMPANIES (Sec 23)**

- (1) Where, during the course of proceedings before any arbitrator or tribunal under the Industrial Disputes Act, 1947 (14 of 1947), or under any corresponding law relating to investigation and settlement of industrial disputes in force in a State and to which any dispute of the nature specified in Sec.22 has been referred, the balance-sheet and the profit and loss account of an employer, being a corporation or a company (other than a banking company), duly audited by the Comptroller and Auditor-General of India or by auditors duly qualified to act as auditors of companies under sub-section (1) of Sec.226 of the Companies Act, 1956 (1 of 1956), are produced before it, then the said authority may presume the statements and the particulars contained in such balance-sheet and profit and loss account to be accurate and it shall not be necessary for the corporation or the company to prove the accuracy of such statements and particulars by the filing of an affidavit or by any other mode:

Provided that where the said Authority is satisfied that the statements and particulars contained in the balance-sheet or the profit and loss account of the corporation or the company are not accurate, it may take such steps as it thinks necessary to find out the accuracy of such statements and particulars.

- (2) When an application is made to the said Authority by any trade union being a party to the dispute or where there is not trade union, by the employees being a party to the dispute, requiring any clarification relating to any item in the balance-sheet or the profit and loss account, it may, after satisfying itself that such clarification is necessary, by order, direct the corporation or, as the case may be, the company, to furnish to the trade union or the employees such clarification within such time as may be specified in the direction and the corporation or, as the case may be, the company shall comply with such direction.

AUDITED ACCOUNTS OF BANKING COMPANIES NOT TO BE QUESTIONED (Sec 24)

- (1) Where any dispute of the nature specified in Sec.22 between an employer, being a banking company, and its employees has been referred to the said authority under that section and during the course of proceedings the accounts of the banking company duly audited are produced before it, the said authority shall not permit any trade union or employees to question the correctness of such accounts, but the trade union or the employees may be permitted to obtain from the banking company such information as is necessary for verifying the amount of bounds due under this Act.
- (2) Nothing contained in sub-section (1) shall enable the trade union or the employees to obtain any information which the banking company is not compelled to furnish under the provisions of Sec. 34-A of the Banking Regulation Act, 1949 (10 of 1949).

AUDIT OF ACCOUNTS OF EMPLOYERS, NOT BEING CORPORATIONS OR COMPANIES (Sec 25)

- (1) Where any dispute of the nature specified in Section 22 between an employer, not being a corporation or a company, and his employees has been referred to the said Authority under that section and the accounts of such employer audited by any auditor duly qualified to act as auditor of Companies under sub-section (1) of Section 226 of the Companies Act, 1956 (1 of 1956), are produced before the said authority, the provisions of Section 23, shall, so far as may be, apply to the accounts so audited.
- (2) When the said Authority finds that the accounts of such employer have not been audited by any such auditor and it is of opinion that an audit of the accounts of such employer is necessary for deciding the question referred to it, then it may, by order, direct the employer to get his accounts audited within such time as may be specified in the direction or within such further time as it thinks fit and thereupon the employer shall comply with such direction.
- (3) Where an employer fails to get the accounts audited under sub-section (2) the said authority may, without prejudice to the provisions of Sec.28 get the accounts audited by such auditor or auditors as it thinks fit.
- (4) When, the accounts are audited under sub-section (2) or sub-section (3) the provisions of Sec.23 shall, so far as may be, apply to the accounts so audited.
- (5) The expenses of, and incidental to, any audit under sub-section (3) (including the remuneration of the auditor or auditors) shall be determined by the said authority (which determination shall be final) and paid by the employer and in default of such payment shall be recoverable from the employer in the manner provided in Sec.21



MAINTENANCE OF REGISTER, RECORDS, ETC

Every employer shall prepare and maintain such registers, records and other documents in such form and in such manner as may be prescribed. (Sec 26)

INSPECTORS (Sec 27)

- (1) The appropriate Government may, by notification in the official Gazette, appoint such persons as it thinks fit to be Inspectors for the purpose of this Act and may define the limits within which they shall exercise jurisdiction.
- (2) Require an employer to furnish such information as he may consider necessary :
 - (a) At any reasonable time and with such assistance, if any, as he thinks fit, enter any establishment or any premises connected therewith and require any one found in charge thereof to produce before him for examination any accounts, books, registers and other documents relating to the employment of persons or the payment of salary or wage or bonus in the establishment;
 - (b) Examine with respect to any matter relevant to any of the purposes aforesaid, the employer, his agent or servant or any other person found in charge of establishment or any premises connected therewith or any person whom the Inspector has reasonable cause to believe to be or to have been an employee in the establishment ;
 - (c) Make copies of, or take extracts from, any book, register or other document maintained in relation to the establishment ;
 - (d) Exercise such other powers as may be prescribed.
- (3) Every Inspector shall be deemed to be a public servant within the meaning of the Indian Penal Code (45 of 1860).
- (4) A person required to produce any accounts, book, register or other document or to give information by an Inspector under sub-section (1) shall be legally bound to do so.
- (5) Nothing contained in this section shall enable an Inspector to require a banking company to furnish or disclose any statement or information or to produce, or give inspection of, any of its books of account or other documents, which a banking company cannot be compelled to furnish, disclose, produce or give inspection of, under the provisions of Sec. 34-A of the Banking Regulation Act, 1949(10 of 1949)].

PENALTIES (Sec 28)

If any person contravenes any of the provisions of the Act or any rule made thereunder, he shall be punishable with imprisonment for a term which may extend upto 6 months or a fine which may extend upto ` 10,000/- or both.

OFFENCES BY COMPANIES (Sec 29)

- (1) If the person committing an offence under this Act is 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 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:

provided that nothing contained in sub-section (1), 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, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be proceeded against and punished accordingly.

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.

**PROTECTION OF ACTION TAKEN UNDER THE ACT. (Sec 31)**

No suit, prosecution or other legal proceeding shall lie against the Government or any officer of the Government for anything which is in good faith done or intended to be done in pursuance of this Act or any rule made thereunder.

SPECIAL PROVISION WITH RESPECT TO PAYMENT OF BONUS LINKED WITH PRODUCTION OR PRODUCTIVITY (Sec 31A)

Notwithstanding anything contained in this Act, -

- (i) Where an agreement or a settlement has been entered into by the employees with their employer before the commencement of the Payment of Bonus (Amendment) Act, 1976 (23 of 1976), or
- (ii) Where the employees enter into any agreement with their employer after such commencement,
For payment of an annual bonus linked with production or productivity in lieu of bonus based on profits payable under this Act, then, such employees shall be entitled to receive bonus due to them under such agreement or settlement, as the case may be :
[(Note: Ins. by Act 66 of 1980, (w.e.f. 21st August, 1980)) Provided that any such agreement or settlement whereby the employees relinquish their right to receive the minimum bonus under Sec.10 shall be null and void in so far as it purports to deprive them of such right :]
[(Note: Subs. by ibid) Provided further that] such employees shall not be entitled to be paid such bonus in excess of twenty per cent, of the salary or wage earned by them during the relevant accounting year.]

ACT NOT TO APPLY TO CERTAIN CLASSES OF EMPLOYEES (Sec 32)

Nothing in this Act shall apply to—

- (i) Employees employed by any insurer carrying on general insurance business and the employees employed by the Life Insurance Corporation of India ;
- (ii) Seaman as defined in Cl. (42) of Sec.3 of the Merchant Shipping Act, 1958 (44 of 1958) ;
- (iii) Employees registered or listed under any scheme made under the Dock Workers (Regulation of Employment) Act, 1948 (9 of 1948), and employed by registered or listed employers ;
- (iv) Employees employed by an establishment engaged in any industry carried on by or under the authority of any department of the Central Government or a State Government or a local Authority ;
- (v) Employees employed by -
 - (a) The Indian Red Cross Society or any other Institution of a like nature (including its branches);
 - (b) Universities and other educational institutions ;
 - (c) Institutions (including hospitals, chambers of commerce and society welfare institutions) established not for purposes of profit ;
 - (i) Employees employed through contractors on building operations ;
 - (ii) (Note: Clause (vii) omitted by Act 66 of 1980, (w.e.f. 21st August, 1980)
 - (iii) Employees employed by the Reserve Bank of India ;
- (iv) Employees employed by -
 - (a) The Industrial Finance Corporation of India;
 - (b) By Financial Corporation established under Sec.3, or any Joint Financial Corporation established under Sec. 3-A of the State Financial Corporations Act, 1951 (63 of 1951) ;
 - (c) The Deposit Insurance Corporation ;
 - (d) [(Note: Subs. by Act 61 of 1981) the National Bank for Agriculture and Rural Development;]
 - (e) The Unit Trust of India ;
 - (f) The Industrial Development Bank of India ;

(Note: Omitted by Act 66 of 1980, (w.e.f. 21st August, 1980))



- (g) Any other financial institution [(Note: Ins. by ibid) Other than a banking company], being an establishment in public sector, which the Central Government may, by notification in the official Gazette, specify having regard to -
 - (i) Its capital structure ;
 - (i) Its objectives and the nature of its activities;
 - (ii) The nature and extent of financial assistance or any concession given to it by the Government; and
 - (iii) Any other relevant factor ;
- (i) (Note: Clause (x) omitted by Act 23 of 1976, Sec.20, (w.e.f. 25th September, 1975)
- (ii) Employees employed by inland water transport establishments operating on routes passing through any other country.

NOTES

Applicability of the provisions of the Bonus Act to employees the Defence ministry canteen stores department. It was held that canteen stores department is an “establishment” engaged in any industry carried on by or under the authority of any department of the Central Government. (Radhu-k-Kallde of Bombay v. Union of India and other (1986) 1 S.C.J.5). **33.** [Act to apply of certain pending dispute regarding payment of bonus.] Rep. by the Payment of Bonus (Amendment) Act, 1976 (23 of 1976), Section 21 (w.e.f. 25th September, 1975).

EMPLOYEES AND EMPLOYERS NOT TO BE PRECLUDED FROM ENTERING INTO AGREEMENTS FOR GRANT OF BONUS UNDER A DIFFERENT FORMULA (Sec 34)

Nothing contained in this Act shall be construed to preclude employees employed in any establishment or class of establishments from entering into agreements with their employer for granting them an account of bonus under a formula which is different for that under this Act :

Provided that no such agreement shall have effect unless it is entered into with the previous approval of the appropriate Government :

Provided further that any such agreement whereby the employees relinquish their right to receive the minimum bonus under sub-section (2-A) of Section 10 shall be null and void in so far as it purports to deprive them of such right :

Provided also that such employees shall not be entitled to be paid bonus in excess of—

- (a) 8.33 per cent of the salary or wage earned by them during accounting year if the employer has no allocable surplus in the accounting year or the amount of such allocable surplus is only so much that, but for the provisions of sub-section (2-A) of Section 10, it would entitle the employees only to receive an amount of bonus which is less than the aforesaid percentage, or
- (b) Twenty per cent, of the salary or wage earned by them during the accounting year.

NOTES

Employer and workmen enter into settlement before Conciliation Officer on 9th October, 1972 within the meaning of Sec.34 (3) of Payment of Bonus Act - On a reference before the tribunal workmen claims three month Salary as customer's bonus or 2% of salary as per the Act - Validity of award directing payment of three months basic wages as on 31st March 1972 instead of 31st March 1970 in term 1 of the Settlement. (Dishegarh Power Supply Co., Ltd. v. The Workmen of Dishegarh Power Supply Co., Ltd., (1986) 3 SCJ 247).

EFFECT OF LAWS AND AGREEMENTS INCONSISTENT WITH THE ACT (Sec 34A)

Subject to the provisions of Sections 31-A and 34, 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 the terms of any award, agreement, settlement or contract of service.

SAVING (Sec 35)

Nothing contained in this Act shall be deemed to affect the provisions of the Coal Mines Provident Fund and Bonus Schemes Act, 1948 (46 of 1948), or of any scheme made there under.

**POWER OF EXEMPTION (Sec 36)**

If the appropriate Government, having regard to the financial position and other relevant circumstances of any establishment or class of establishments, is of opinion that it will not be in public interest to apply all or any of the provisions of this Act thereto, it may, by notification in the official Gazette, exempt for such period as may be specified therein and subject to such conditions as it may think fit to impose, such establishment or class of establishments from all or any of the provisions of this Act.

NOTES

The Court has jurisdiction to consider whether the powers under Section 36 has been properly exercised by the Government.

Consideration of the profits for one previous year cannot amount to consideration of “the financial position” of an establishment within the terms of Section 36 of the Bonus Act. (*M/s, Fashan Electric Dry Cleaners v. The Government of A.P.* (1977) 1 An. A.W.R.27).

37. [Power to remove difficulties] Rep. by the Payment of Bonus (Amendment) Act, 1976 (23 of 1976), Section 23 (w.e.f. 25th September, 1975).

POWER OF MAKE RULES (Sec 38)

- (1) The Central Government may make rules for the purpose of carrying into effect the provision of this Act.
- (2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for—
 - (a) The authority for granting permission under the proviso to sub-clause (iii) of Cl. (I) of Sec.2;
 - (b) The preparation of registers, records and other document and the form and manner in which such registers, records and documents may be maintained under Sec.26 ;
 - (c) The powers which may be exercised by an inspector under Cl. (e) of sub-section (2) of Sec.27;
 - (d) Any other matter which is to be, or may be prescribed.
- (3) Every rule made under this section 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 [(Note: Subs. by Act 23 of 1976, (w.e.f. 25th September, 1975) or in two or more successive session], and if before the expiry of the session [(Note: Subs. by Sec.21, *ibid*, (w.e.f. 25th September, 1975) 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.

APPLICATION OF CERTAIN LAWS NOT BARRED (Sec 39)

Save as otherwise expressly provided, the provisions of this Act shall be in addition to and not in derogation of the industrial Disputes Act, 1947 (14 of 1947) or any corresponding law relating The Orient Tavern investigation and settlement of industrial disputes in force in a State.



3.8. THE PAYMENT OF GRATUITY ACT, 1972

An Act to provide for a scheme for the payment of gratuity to employees engaged in factories, mines, oilfields, plantations, ports, railway companies, shops or other establishments and for matters connected therewith or incidental thereto.—

1. EXTENT

- (1) This Act may be called the Payment of Gratuity Act, 1972.
- (2) It extends to the whole of India : Provided that in so far as it relates to plantations or ports, it shall not extend to the State of Jammu and Kashmir.
- (3) It shall apply to—
 - (a) every factory, mine, oilfield, plantation, port and railway company;
 - (b) every shop or establishment within the meaning of any law for the time being in force in relation to shops and establishments in a State, in which ten or more persons are employed, or were employed, on any day of the preceding twelve months;
 - (c) such other establishments or class of establishments, in which ten or more employees are employed, or were employed, on any day of the preceding twelve months, as the Central Government may, by notification, specify in this behalf.
- (3A) A shop or establishment to which this Act has become applicable shall continue to be governed by this Act notwithstanding that the number of persons employed therein at any time after it has become so applicable falls below ten.
- (4) It shall come into force on such date as the Central Government may, by notification, appoint.

2. BASIC CONCEPTS

In this Act, unless the context otherwise requires,—

- (a) “appropriate Government”

means,—

- (i) in relation to an establishment –

- (a) belonging to, or under the control of, the Central Government,
- (b) having branches in more than one State,
- (c) of a factory belonging to, or under the control of, the Central Government,
- (d) of a major port, mine, oilfield or railway company, the Central Government,
- (ii) in any other case, the State Government;

- (b) “completed year of service”

means continuous service for one year;

- (c) “continuous service”

means continuous service as defined in section 2A;

- (d) “controlling authority”

means an authority appointed by the appropriate Government under section 3;

- (e) “employee”

means any person (other than an apprentice) employed on wages, in any establishment, factory, mine, oilfield, plantation, port, railway company or shop, to do any skilled, semi-skilled, or unskilled, manual, supervisory, technical or clerical work, whether the terms of such employment are express or implied, and whether or not such person is employed in a managerial or administrative capacity, but does not include any such person who holds a post under the Central Government or a State Government and is governed by any other Act or by any rules providing for payment of gratuity.



- (f) “employer”
means, in relation to any establishment, factory, mine, oilfield, plantation, port, railway company or shop—
- (i) belonging to, or under the control of, the Central Government or a State Government, a person or authority appointed by the appropriate Government for the supervision and control of employees, or where no person or authority has been so appointed, the head of the Ministry or the Department concerned,
- (ii) belonging to, or under the control of, any local authority, the person appointed by such authority for the supervision and control of employees or where no person has been so appointed, the chief executive officer of the local authority,
- (iii) in any other case, the person, who, or the authority which, has the ultimate control over the affairs of the establishment, factory, mine, oilfield, plantation, port, railway company or shop, and where the said affairs are entrusted to any other person, whether called a manager, managing director or by any other name, such person;
- (g) “factory”
Means has the meaning assigned to it in clause (m) of section 2 of the Factories Act, 1948 (63 of 1948);
- (h) “family”,
Means in relation to an employee, shall be deemed to consist of –
- (i) in the case of a male employee, himself, his wife, his children, whether married or unmarried, his dependent parents and the dependent parents of his wife and the widow and children of his predeceased son, if any,
- (ii) in the case of a female employee, herself, her husband, her children, whether married or unmarried, her dependent parents and the dependent parents of her husband and the widow and children of her predeceased son, if any :
- Explanation :** Where the personal law of an employee permits the adoption by him of a child, any child lawfully adopted by him shall be deemed to be included in his family, and where a child of an employee has been adopted by another person and such adoption is, under the personal law of the person making such adoption, lawful, such child shall be deemed to be excluded from the family of the employee;
- (i) “major port” has the meaning assigned to it in clause (8) of section 3 of the Indian Ports Act, 1908 (15 of 1908);
- (j) “mine” has the meaning assigned to it in clause (j) of sub-section (1) of section 2 of the Mines Act, 1952 (35 of 1952);
- (k) “notification” means a notification published in the Official Gazette;
- (l) “oilfield” has the meaning assigned to it in clause (e) of section 3 of the Oilfields (Regulation and Development) Act, 1948 (53 of 1948);
- (m) “plantation” has the meaning assigned to it in clause (f) of section 2 of the Plantations Labour Act, 1951 (69 of 1951);
- (n) “port” has the meaning assigned to it in clause (4) of section 3 of the Indian Ports Act, 1908 (15 of 1908);
- (o) “prescribed” means prescribed by rules made under this Act;
- (p) “railway company” has the meaning assigned to it in clause (5) of section 3 of the Indian Railways Act, 1890 (9 of 1890);
- (q) “retirement” means termination of the service of an employee otherwise than on superannuation;
- (r) “superannuation”, in relation to an employee, means the attainment by the employee of such age as is fixed in the contract or conditions of service at the age on the attainment of which the employee shall vacate the employment;
- (s) “wages” means all emoluments which are earned by an employee while on duty or on leave in accordance with the terms and conditions of his employment and which are paid or are payable to him in cash and includes dearness allowance but does not include any bonus, commission, house rent allowance, overtime wages and any other allowance.



2A. CONTINUOUS SERVICE

For the purposes of this Act,—

- (1) an employee shall be said to be in continuous service for a period if he has, for that period, been in uninterrupted service, including service which may be interrupted on account of sickness, accident, leave, absence from duty without leave (not being absence in respect of which an order treating the absence as break in service has been passed in accordance with the standing order, rules or regulations governing the employees of the establishment), lay off, strike or a lock-out or cessation of work not due to any fault of the employee, whether such uninterrupted or interrupted service was rendered before or after the commencement of this Act.
- (2) where an employee (not being an employee employed in a seasonal establishment) is not in continuous service within the meaning of clause (1), for any period of one year or six months, he shall be deemed to be in continuous service under the employer—
 - (a) for the said period of one year, if the employee during the period of twelve calendar months preceding the date with reference to which calculation is to be made, has actually worked under the employer for not less than—
 - (i) one hundred and ninety days, in the case of an employee employed below the ground in a mine or in an establishment which works for less than six days in a week; and
 - (ii) two hundred and forty days, in any other case;
 - (b) for the said period of six months, if the employee during the period of six calendar months preceding the date with reference to which the calculation is to be made, has actually worked under the employer for not less than—
 - (i) ninety-five days, in the case of an employee employed below the ground in a mine or in an establishment which works for less than six days in a week; and
 - (ii) one hundred and twenty days, in any other case;

Explanation : For the purpose of clause (2), the number of days on which an employee has actually worked under an employer shall include the days on which—

- (i) he has been laid-off under an agreement or as permitted by standing orders made under the Industrial Employment (Standing Order's) Act, 1946 (20 of 1946), or under the Industrial Disputes Act, 1947 (14 of 1947), or under any other law applicable to the establishment;
 - (ii) he has been on leave with full wages, earned in the previous year;
 - (iii) he has been absent due to temporary disablement caused by accident arising out of and in the course of his employment; and
 - (iv) in the case of a female, she has been on maternity leave; so, however, that the total period of such maternity leave does not exceed twelve weeks.
- (3) where an employee employed in a seasonal establishment, is not in continuous service within the meaning of clause (1), for any period of one year or six months, he shall be deemed to be in continuous service under the employer for such period if he has actually worked for not less than seventy-five per cent of the number of days on which the establishment was in operation during such period

CONTROLLING AUTHORITY (Sec 3)

The appropriate Government may, by notification, appoint any officer to be a controlling authority, who shall be responsible for the administration of this Act and different controlling authorities may be appointed for different areas.

PAYMENT OF GRATUITY (Sec 4)

- (1) Gratuity shall be payable to an employee on the termination of his employment after he has rendered continuous service for not less than five years,—
 - (a) on his superannuation, or
 - (b) on his retirement or resignation, or
 - (c) on his death or disablement due to accident or disease : Provided that the completion of continuous



service of five years shall not be necessary where the termination of the employment of any employee is due to death or disablement :

Provided further that in the case of death of the employee, gratuity payable to him shall be paid to his nominee or, if no nomination has been made, to his heirs, and where any such nominees or heirs is a minor, the share of such minor, shall be deposited with the controlling authority who shall invest the same for the benefit of such minor in such bank or other financial institution, as may be prescribed, until such minor attains majority.

Explanation : For the purposes of this section, disablement means such disablement as incapacitates an employee for the work which he was capable of performing before the accident or disease resulting in such disablement.

- (2) For every completed year of service or part thereof in excess of six months, the employer shall pay gratuity to an employee at the rate of fifteen days' wages based on the rate of wages last drawn by the employee concerned : Provided that in the case of a piece-rated employee, daily wages shall be computed on the average of the total wages received by him for a period of three months immediately preceding the termination of his employment, and, for this purpose, the wages paid for any overtime work shall not be taken into account :

Provided further that in the case of an employee who is employed in a seasonal establishment and who is not so employed throughout the year, the employer shall pay the gratuity at the rate of seven days' wages for each season.

Explanation : In the case of a monthly rated employee, the fifteen days' wages shall be calculated by dividing the monthly rate of wages last drawn by him by twenty-six and multiplying the quotient by fifteen.

- (3) The amount of gratuity payable to an employee shall not exceed three lakhs and fifty thousand rupees.
- (4) For the purpose of computing the gratuity payable to an employee who is employed, after his disablement, on reduced wages, his wages for the period preceding his disablement shall be taken to be the wages received by him during that period, and his wages for the period subsequent to his disablement shall be taken to be the wages as so reduced.
- (5) Nothing in this section shall affect the right of an employee to receive better terms of gratuity under any award or agreement or contract with the employer.
- (6) Notwithstanding anything contained in sub-section (1),—
- (a) the gratuity of an employee, whose services have been terminated for any act, willful omission or negligence causing any damage or loss to, or destruction of, property belonging to the employer, shall be forfeited to the extent of the damage or loss so caused.
 - (b) the gratuity payable to an employee may be wholly or partially forfeited—
 - (i) if the services of such employee have been terminated for his riotous or disorderly conduct or any other act of violence on his part, or
 - (ii) if the services of such employee have been terminated for any act which constitutes an offence involving moral turpitude, provided that such offence is committed by him in the course of his employment.

COMPULSORY INSURANCE (Sec 4A)

- (1) With effect from such date as may be notified by the appropriate Government in this behalf, every employer, other than an employer or an establishment belonging to, or under the control of, the Central Government or a State Government, shall, subject to the provisions of sub-section (2), obtain an insurance in the manner prescribed, for his liability for payment towards the gratuity under this Act, from the Life Insurance Corporation of India established under the Life Insurance Corporation of India Act, 1956 (31 of 1956) or any other prescribed insurer : Provided that different dates may be appointed for different establishments or class of establishments or for different areas.
- (2) The appropriate Government may, subject to such conditions as may be prescribed, exempt every employer who had already established an approved gratuity fund in respect of his employees and who desires to continue such arrangement, and every employer employing five hundred or more persons who establishes an approved gratuity fund in the manner prescribed from the provisions of sub-section (1).



- (3) For the purpose of effectively implementing the provisions of this section, every employer shall within such time as may be prescribed get his establishment registered with the controlling authority in the prescribed manner and no employer shall be registered under the provisions of this section unless he has taken an insurance referred to in sub-section (1) or has established an approved gratuity fund referred to in sub-section (2).
- (4) The appropriate Government may, by notification, make rules to give effect to the provisions of this section and such rules may provide for the composition of the Board of Trustees of the approved gratuity fund and for the recovery by the controlling authority of the amount of the gratuity payable to an employee from the Life Insurance Corporation of India or any other insurer with whom an insurance has been taken under sub-section (1), or as the case may be, the Board of Trustees of the approved gratuity fund.
- (5) Where an employer fails to make any payment by way of premium to the insurance referred to in sub-section (1) or by way of contribution to an approved gratuity fund referred to in sub-section (2), he shall be liable to pay the amount of gratuity due under this Act (including interest, if any, for delayed payments) forthwith to the controlling authority.
- (6) Whoever contravenes the provisions of sub-section (5) shall be punishable with fine which may extend to ten thousand rupees and in the case of a continuing offence with a further fine which may extend to one thousand rupees for each day during which the offence continues.

Explanation : In this section “approved gratuity fund” shall have the same meaning as in clause (5) of section 2 of the Income-tax Act, 1961 (43 of 1961).

POWER TO EXEMPT (Sec 5)

- (1) The appropriate Government may, by notification, and subject to such conditions as may be specified in the notification, exempt any establishment, factory, mine, oilfield, plantation, port, railway company or shop to which this Act applies from the operation of the provisions of this Act if, in the opinion of the appropriate Government, the employees in such establishment, factory, mine, oilfield, plantation, port, railway company or shop are in receipt of gratuity or pensionary benefits not less favourable than the benefits conferred under this Act.
- (2) The appropriate Government may, by notification and subject to such conditions as may be specified in the notification, exempt any employee or class of employees employed in any establishment, factory, mine, oilfield, plantation, port, railway company or shop to which this Act applies from the operation of the provisions of this Act, if, in the opinion of the appropriate Government, such employee or class of employees are in receipt of gratuity or pensionary benefits not less favourable than the benefits conferred under this Act.
- (3) A notification issued under sub-section (1) or sub-section (2) may be issued retrospectively a date not earlier than the date of commencement of this Act, but no such notification shall be issued so as to prejudicially affect the interests of any person.

NOMINATION (Sec 6)

- (1) Each employee, who has completed one year of service, shall make, within such time, in such form and in such manner, as may be prescribed, nomination for the purpose of the second proviso to sub-section (1) of section 4.
- (2) An employee may in his nomination, distribute the amount of gratuity payable to him, under this Act amongst more than one nominee.
- (3) If an employee has a family at the time of making a nomination, the nomination shall be made in favour of one or more members of his family, and any nomination made by such employee in favour of a person who is not a member of his family, shall be void.
- (4) If at the time of making a nomination the employee has no family, the nomination may be made in favour of any person or persons but if the employee subsequently acquires a family, such nomination shall forthwith become invalid and the employee shall make, within such time as may be prescribed, a fresh nomination in favour of one or more members of his family.
- (5) A nomination may, subject to the provisions of sub-sections (3) and (4), be modified by an employee at any time, after giving to his employer a written notice in such form and in such manner as may be prescribed, of his intention to do so.



- (6) If a nominee predeceases the employee, the interest of the nominee shall revert to the employee who shall make a fresh nomination, in the prescribed form, in respect of such interest.
- (7) Every nomination, fresh nomination or alteration of nomination, as the case may be, shall be sent by the employee to his employer, who shall keep the same in his safe custody.

DETERMINATION OF THE AMOUNT OF GRATUITY (Sec 7)

- (1) A person who is eligible for payment of gratuity under this Act or any person authorised, in writing, to act on his behalf shall send a written application to the employer, within such time and in such form, as may be prescribed, for payment of such gratuity.
- (2) As soon as gratuity becomes payable, the employer shall, whether an application referred to in sub-section (1) has been made or not, determine the amount of gratuity and give notice in writing to the person to whom the gratuity is payable and also to the controlling authority specifying the amount of gratuity so determined.
- (3) The employer shall arrange to pay the amount of gratuity within thirty days from the date it becomes payable to the person to whom the gratuity is payable.
- (3A) If the amount of gratuity payable under sub-section (3) is not paid by the employer within the period specified in sub-section (3), the employer shall pay, from the date on which the gratuity becomes payable to the date on which it is paid, simple interest at such rate, not exceeding the rate notified by the Central Government from time to time for repayment of long-term deposits, as that Government may, by notification specify : Provided that no such interest shall be payable if the delay in the payment is due to the fault of the employee and the employer has obtained permission in writing from the controlling authority for the delayed payment on this ground.
- (4)
 - (a) If there is any dispute as to the amount of gratuity payable to an employee under this Act or as to the admissibility of any claim of, or in relation to, an employee for payment of gratuity, or as to the person entitled to receive the gratuity, the employer shall deposit with the controlling authority such amount as he admits to be payable by him as gratuity.
 - (b) Where there is a dispute with regard to any matter or matters specified in clause (a), the employer or employee or any other person raising the dispute may make an application to the controlling authority for deciding the dispute.
 - (c) The controlling authority shall, after due inquiry and after giving the parties to the dispute a reasonable opportunity of being heard, determine the matter or matters in dispute and if, as a result of such inquiry any amount is found to be payable to the employee, the controlling authority shall direct the employer to pay such amount or, as the case may be, such amount as reduced by the amount already deposited by the employer.
 - (d) The controlling authority shall pay the amount deposited, including the excess amount, if any, deposited by the employer, to the person entitled thereto.
 - (e) As soon as may be after a deposit is made under clause (a), the controlling authority shall pay the amount of the deposit—
 - (i) to the applicant where he is the employee; or
 - (ii) where the applicant is not the employee, to the nominee or, as the case may be, the guardian of such nominee or heir of the employee if the controlling authority is satisfied that there is no dispute as to the right of the applicant to receive the amount of gratuity.
- (5) For the purpose of conducting an inquiry under sub-section (4), the controlling authority shall have the same powers as are vested in a court, while trying a suit, under the Code of Civil Procedure, 1908 (5 of 1908), in respect of the following matters, namely —
 - (a) enforcing the attendance of any person or 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.
- (6) Any inquiry under this section shall be a judicial proceeding within the meaning of sections 193 and 228, and for the purpose of section 196, of the Indian Penal Code, 1860 (45 of 1860).



- (7) Any person aggrieved by an order under sub-section (4) may, within sixty days from the date of the receipt of the order, prefer an appeal to the appropriate Government or such other authority as may be specified by the appropriate Government in this behalf : Provided that the appropriate Government or the appellate authority, as the case may be, may, if it is satisfied that the appellant was prevented by sufficient cause from preferring the appeal within the said period of sixty days, extend the said period by a further period of sixty days.

Provided further that no appeal by an employer shall be admitted unless at the time of preferring the appeal, the appellant either produces a certificate of the controlling authority to the effect that the appellant has deposited with him an amount equal to the amount of gratuity required to be deposited under sub-section (4), or deposits with the appellate authority such amount.

- (8) The appropriate Government or the appellate authority, as the case may be, may, after giving the parties to the appeal a reasonable opportunity of being heard, confirm, modify or reverse the decision of the controlling authority.

INSPECTORS (Sec 7A)

- (1) The appropriate Government may, by notification, appoint as many Inspectors, as it deems fit, for the purposes of this Act.
- (2) The appropriate Government may, by general or special order, define the area to which the authority of an Inspector so appointed shall extend and where two or more Inspectors are appointed for the same area, also provide, by such order, for the distribution or allocation of work to be performed by them under this Act.
- (3) Every Inspector shall be deemed to be a public servant within the meaning of section 21 of the Indian Penal Code, 1860 (45 of 1860).

POWERS OF INSPECTORS (Sec 7B)

- (1) Subject to any rules made by the appropriate Government in this behalf, an Inspector may, for the purpose of ascertaining whether any of the provisions of this Act or the conditions, if any, of any exemption granted thereunder, have been complied with, exercise all or any of the following powers, namely—
- (a) require an employer to furnish such information as he may consider necessary;
 - (b) enter and inspect, at all reasonable hours, with such assistants (if any), being persons in the service of the Government or local or any public authority, as he thinks fit, any premises or place in any factory, mine, oilfield, plantation, port, railway company, shop or other establishment to which this Act applies, for the purpose of examining any register, record or notice or other document required to be kept or exhibited under this Act or the rules made thereunder, or otherwise kept or exhibited in relation to the employment of any person or the payment of gratuity to the employees, and require the production thereof for inspection;
 - (c) examine with respect to any matter relevant to any of the purposes aforesaid, the employer or any person whom he finds in such premises or place and who, he has reasonable cause to believe, is an employee employed therein;
 - (d) make copies of, or take extracts from, any register, record, notice or other document, as he may consider relevant, and where he has reason to believe that any offence under this Act has been committed by an employer, search and seize with such assistance as he may think fit, such register, record, notice or other document as he may consider relevant in respect of that offence;
 - (e) exercise such other powers as may be prescribed.
- (2) Any person required to produce any register, record, notice or other document or to give any information by an Inspector under sub-section (1) shall be deemed to be legally bound to do so within the meaning of sections 175 and 176 of the Indian Penal Code 1860 (45 of 1860).
- (3) The provisions of the Code of Criminal Procedure, 1973 (2 of 1974) shall so far as may be, apply to any search or seizure under this section as they apply to any search or seizure made under the authority of a warrant issued under section 94 of that Code.

**RECOVERY OF GRATUITY (Sec 8)**

If the amount of gratuity payable under this Act is not paid by the employer, within the prescribed time, to the person entitled thereto, the controlling authority shall, on an application made to it in this behalf by the aggrieved person, issue a certificate for that amount to the Collector, who shall recover the same, together with compound interest thereon at such rate as the Central Government may, by notification, specify, from the date of expiry of the prescribed time, as arrears of land revenue and pay the same to the person entitled thereto :

Provided that the controlling authority shall, before issuing a certificate under this section, give the employer a reasonable opportunity of showing cause against the issue of such certificate:

Provided further that the amount of interest payable under this section shall, in no case exceed the amount of gratuity payable under this Act.

PENALTIES (Sec 9)

- (1) Whoever, for the purpose of avoiding any payment to be made by himself under this Act or of enabling any other person to avoid such payment, knowingly makes or causes to be made any false statement or false representation shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to ten thousand rupees or with both.
- (2) An employer who contravenes, or makes default in complying with, any of the provisions of this Act or any rule or order made thereunder shall be punishable with imprisonment for a term which shall not be less than three months but which may extend to one year, or with fine which shall not be less than ten thousand rupees but which may extend to twenty thousand rupees, or with both :

Provided that where the offence relates to non-payment of any gratuity payable under this Act, the employer shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to two years unless the court trying the offence, for reasons to be recorded by it in writing, is of opinion that a lesser term of imprisonment or the imposition of a fine would meet the ends of justice.

10. EXEMPTION OF EMPLOYER FROM LIABILITY IN CERTAIN CASES

Where an employer is charged with an offence punishable under this Act, he shall be entitled, upon complaint duly made by him and on giving to the complainant not less than three clear days' notice in writing of his intention to do so, to have any other person whom he charges as the actual offender brought before the court at the time appointed for hearing the charge; and if, after the commission of the offence has been proved, the employer proves to the satisfaction of the court - (a) that he has used due diligence to enforce the execution of this Act, and

(b) that the said other person committed the offence in question without his knowledge, consent or connivance, that other person shall be convicted of the offence and shall be liable to the like punishment as if he were the employer and the employer shall be discharged from any liability under this Act in respect of such offence :

Provided that in seeking to prove as aforesaid, the employer may be examined on oath and his evidence and that of any witness whom he calls in his support shall be subject to cross-examination on behalf of the person he charges as the actual offender and by the prosecutor :

Provided further that, if the person charged as the actual offender by the employer cannot be brought before the court at the time appointed for hearing the charge, the court shall adjourn the hearing from time to time for a period not exceeding three months and if by the end of the said period the person charged as the actual offender cannot still be brought before the court, the court shall proceed to hear the charge against the employer and shall, if the offence be proved, convict the employer.

COGNIZANCE OF OFFENCES (Sec 11)

- (1) No court shall take cognizance of any offence punishable under this Act save on a complaint made by or under the authority of the appropriate Government : Provided that where the amount of gratuity has not been paid, or recovered, within six months from the expiry of the prescribed time, the appropriate Government shall authorise the controlling authority to make a complaint against the employer, whereupon the controlling authority shall, within fifteen days from the date of such authorisation, make such complaint to a Magistrate having jurisdiction to try the offence.



- (2) No court inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of the first class shall try any offence punishable under this Act.

PROTECTION OF ACTION TAKEN IN GOOD FAITH (Sec 12)

No suit or other legal proceeding shall lie against the controlling authority or any other person 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.

PROTECTION OF GRATUITY (Sec 13)

No gratuity payable under this Act and no gratuity payable to an employee employed in any establishment, factory, mine, oilfield, plantation, port, railway company or shop exempted under section 5 shall be liable to attachment in execution of any decree or order of any civil, revenue or criminal court.

ACT TO OVERRIDE OTHER ENACTMENTS, ETC (Sec 14)

The provisions of this Act or any rule made thereunder shall have effect notwithstanding anything inconsistent therewith contained in any enactment other than this Act or in any instrument or contract having effect by virtue of any enactment other than this Act.

POWER TO MAKE RULES (Sec 15)

- (1) The appropriate Government may, by notification make rules for the purpose of carrying out the provisions of this Act.
- (2) 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.

Gratuity - Meaning

Gratuity is a lump sum payment made by the employer as a mark of recognition of the service rendered by the employee when he retires or leaves service.

Applicability

The Act is applicable to every factory, shop or an establishment, in which ten or more persons are employed, or were employed on any day of the proceeding twelve months. Every employee irrespective of his salary will be entitled to gratuity. Once the Act becomes applicable, it shall continue to be governed by the provisions notwithstanding that the number of persons employed therein have fallen below ten.

Eligibility

An employee is eligible for receiving gratuity payment only after he has completed five years of continuous service. He is said to be in continuous service when he has provided uninterrupted service during that period. on super annuation or on his retirement or resignation or death or disablement due to accident or disease.

This condition of five years is not necessary if the termination of the employment of an employee is due to death or disablement. However, interruption on account of sickness, accident, leave, lay-off, strike, lockout, cessation of work not due to any fault of the employee will not be considered as a break in service. (Section 4)

Amount Payable

Gratuity is payable @ 15 days wages for every year of completed service or part thereof in excess of six months. In case of seasonal establishment, gratuity is payable @ 7 days wages for each season. Wages will include basic and D.A. The daily wages in respect of piece rated employees are to be computed on the average of the total wages received by an employee for a period of three months. The maximum amount of Gratuity payable is ` 3.5 lakhs.

**Amount - When payable**

Any person to whom the gratuity amount is payable shall make a written application to the employer. The employer is required to determine the amount of gratuity payable and give notice in writing to the person to whom the same is payable and to the controlling authority thereby specifying the amount of gratuity payable. The employer is under obligation to pay the gratuity amount within 30 days from the date it becomes payable. Simple interest at the rate of 10% p.a. is payable on the expiry of the said period. If there is a dispute as regards the amount of gratuity payable or with regards the person to whom it is payable, the employer shall deposit the said amount payable with the controlling Authority. If the gratuity is not paid within the prescribed time, the controlling authority shall after due inquiry determine the amount payable and direct the employer to deposit the said amount. If an employer agrees to provide more benefits than the benefits flowing from the Act, he can always have a private scheme.

Nomination

Every employee who completes one year of service is eligible to file nomination in Form - F in duplicate to the employer. In case of death of employee, a nominee or legal heir shall submit the application in Form J or K for claim amount. The employer shall pay the gratuity within 30 days of the receipt of the application. If no nomination has been made, it shall be paid to the legal heirs of the deceased employee or if the heirs are minor, the share of such minor shall be deposited by the controlling authority with a bank till he attains majority.

Forfeiture

Gratuity can be forfeited for any employee whose services have been terminated for any act, willful omission or negligence causing damage or destruction to the property belonging to the employer. It can also be forfeited for any act which constitutes an offence involving moral turpitude. Where services have not been terminated on any of the above grounds, the employer cannot withhold gratuity due to the employee. Where the land of the employer is not vacated by the employee, gratuity cannot be withheld.

Obligation of the Employer

The employer is usually required to submit a notice of opening of an establishment to the controlling authority of the area in form A containing names and addresses of the establishment, employer, number of persons employed, nature of business etc.

The employer shall display conspicuously a notice at or near the main entrance of the establishment in bold letters in English and in a language understood by the majority of employees.

It is the duty of the employer to determine the amount of gratuity as soon as it becomes payable. Failure to do so shall render him liable to pay the interest at the prevailing rate from time taken.

To obtain insurance in the prescribed manner for his liability for payment of gratuity under the Act or establish approved gratuity fund in the prescribed manner.

Penalties

If any person makes a false statement for the purpose of avoiding any payment to be made by him under this Act he shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to ten thousand rupees or with both. If an employer contravenes any provision of the Act, he shall be punishable with imprisonment for a term which shall not be less than three months but which may extend to one year or with a fine, which may vary from ten thousand rupees to twenty thousand rupees.

No court shall take cognizance of any offence punishable under this Act save on a complaint made by or under the authority of the appropriate Government :

Provided that where the amount of gratuity has not been paid, or recovered, within six months from the expiry of the prescribed time, the appropriate Government shall authorise the controlling authority to make a complaint against the employer, whereupon the controlling authority shall, within fifteen days from the date of such authorisation, make such complaint to a Magistrate having jurisdiction to try the offence.

No court inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of the first class shall try any offence punishable under this Act.



3.9. CONSUMER PROTECTION ACT, 1986

1. The preamble to the Act states that the Act is legislated 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.

An Act 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.

SHORT TITLE, EXTENT, COMMENCEMENT AND APPLICATION

- (1) This Act may be called the Consumer Protection Act, 1986.
- (2) It extends to the whole of India except the State of Jammu and Kashmir.
- (3) It shall come into force on such date 1 as the Central Government may, by notification appoint and different dates may be appointed for different States and for different provisions of this Act.
- (4) Save as otherwise expressly provided by the Central Government, by notification, this Act shall apply to all goods and services.

2. ESTABLISHMENT OF DISPUTES REDRESSAL AGENCIES

The Act provides for a three tier system for adjudicating the consumer disputes.

a. District Forum.

b. State Commission.

c. National Commission.

Definitions

- (1) In this Act, unless the context otherwise requires,-
 - (a) "Appropriate laboratory" means a laboratory or organisation-
 - (i) Recognized by the Central Government;
 - (ii) Recognized by a State Government, subject to such guidelines as may be prescribed by the Central Government in this behalf; or
 - (iii) 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;
 - (aa) "Branch office" means—
 - (i) Any establishment described as a branch by the opposite party; or
 - (ii) Any establishment carrying on either the same or substantially the same activity as that carried on by the head office of the establishment;
 - (b) "Complainant" means—
 - (i) A consumer; or
 - (ii) Any voluntary consumer association registered under the companies Act, 1956 (1 of 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;
 - (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;
 - (c) "Complaint" under Consumer Protection Act, 1986 means any allegation in writing made 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) Service 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 service mentioned in the complaint, a price in excess of the price in excess of the price-
 - (a) Fixed by or under any law for the time being in force;
 - (b) Displayed on the goods or any package containing such goods;
 - (c) Displayed on the price list exhibited by him by or under any law for the time being in force;
 - (d) Agreed between the parties;
- (v) Goods which will be hazardous to life and safety when used are being offered for sale to the public;-
 - (a) 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;
 - (b) If the trader could have known with due diligence that the goods so offered are unsafe to the public;]
- (vi) Service 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.
- (d) "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 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
 - (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 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];

[Explanation- For the purposes of this sub-clause "commercial purpose" does not include use by a consumer of goods bought and used by him and services availed by him exclusively for the purposes of earning his livelihood, by means of self-employment;]

- (e) "Consumer dispute" means a dispute where the person against whom a complaint has been made, denies or disputes the allegations contained in the complaint;
- (f) "Defect" means any fault, imperfection or short coming 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;
- (g) "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;
- (h) "District Forum" means a Consumer Disputes Redressal Forum established under Cl. (a) of sec. 9;
- (i) "Goods" means goods as defined in the Sale of Goods Act, 1930 (3 of 1930);
- (j) "Manufacturer" means a person who-
 - (i) Makes or manufactures any goods or parts thereof; or
 - (ii) Does not make or manufacture any goods but assembles parts thereof, made or manufactured by others; or
 - (iii) Puts or causes to be put his own mark on any goods made or manufactured by any other manufacturer.



Explanation- Where a manufacturer despatches any goods or part thereof to any branch office maintained by him, such branch office shall not be deemed to be the manufacturer even though the parts so despatched to it are assembled at such branch office and are sold or distributed from such branch office:

- [(j) “Member” includes the President and a member of the National commission
or a State Commission or a District Forum, as the case may be;]
- (k) “National Commission” means the National Consumer Disputes Redressal Commission established under CI. (c) of sec. 9;
- (l) “National” means a notification published in the official Gazette;
- (m) “Person” includes, -
 - (i) A firm whether registered or not;
 - (ii) A Hindu undivided family;
 - (iii) A Co-operative society;
 - (iv) Every other association of persons whether registered under the societies Registration Act, 1860 (21 of 1860), or not;
- (n) “Prescribed” means prescribed by the rules made by the State Government, or as the case may be, the Central Government under this Act;
- [(nn) “regulation” means the regulations made by the national Commission under this Act;
- [(nnn) “restrictive trade practice” means a trade practice which tends to being about manipulation of price or its conditions of delivery or to affect flow of supplies in the market relating to goods or service in such a manner as to impose on the consumers unjustified costs or restrictions and shall include—
 - (a) delay beyond the period agreed to be 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.]
- (o) “Services” means 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;
- [(oo) “spurious goods and services” mean such goods and services which are claimed to be genuine but they are actually not so,]
- (p) “State Commission” means a Consumer Disputes Redressal Commission established in a State under CI (b) of Sec. 9;
- (q) “Trader” in relation to any goods means “ a person who sells or distributes any goods for sale and includes the manufacturer thereof, and where such goods are sold or distributed in package form, includes the packer thereof”;
- (r) “Unfair trade practice” means a trade practice which, for the purpose of promoting the sale, use or supply of any goods or for the provision of any service, adopts any unfair method or unfair or deceptive practice including any of the following practices, namely:
 - (1) The practice of making any statement, whether orally or in writing or by visible representation which, -
 - (i) Falsely represents that the goods are of a particular standard, quality, quantity; grade-composition, style or model;
 - (ii) Falsely represents that the service of a particular standard, quality or grade;
 - (iii) Falsely represents any re-built, second-hand, renovated, reconditioned or old goods as new goods;
 - (iv) Represents that the goods or service have sponsorship, approval, performance, characteristics, accessories, uses or benefits which such goods or service do not have;
 - (v) Represents that the seller or the supplier has a sponsorship or approval or affiliation which such seller or supplier does not have



- (vi) Makes a false or misleading representation concerning the need for, or the usefulness of, any goods or service;
- (vii) Gives to the public any warranty or guarantee of the performance, efficacy or length of life of a product or of any goods that is not based on an adequate or proper test thereof Provided that where a defence is raised to the effect that such warranty or guarantee is based on adequate or proper test, the burden of proof of such defence shall lie on the person raising such defence;
- (viii) Makes to the public a representation in a form that purports to be -
 - (i) A warranty or guarantee of a product or of any goods or service; or
 - (ii) A promise to replace, maintain or repair an article or any part thereof or to repeat or continue a service until it has achieved a specified result, if such purported warranty or guarantee or promise is materially misleading or if there is no reasonable prospect that such warranty, guarantee or promise will be carried out;
 - (ix) Materially misleads the public concerning the price at which a product or like products or goods or service, have been or are, ordinarily sold or provided, and, for this purpose, a representation as to price shall be deemed to refer to the price at which the product or goods or service has or have been sold by sellers or provided by suppliers generally in the relevant market unless it is clearly specified to be the price at which the product has been sold or services have been provided by the person by whom or on whose behalf the representation is made;
 - (x) Gives false or misleading facts disparaging the goods, services or trade of another person;

Explanation : For the purposes of CI. (1), a statement that is—

- (a) Expressed on an article offered or displayed for sale, or on its wrapper or container; or
- (b) Expressed on anything attached to, inserted in, or accompanying an article offered or displayed for sale or on anything on which the article is mounted for display or sale; or
- (c) Contained in or on anything is sold, sent, delivered, transmitted or in any other manner whatsoever made available to a member of the public,
Shall be deemed to be a statement made to the public by, and only by, the person who had caused the statement to be so expressed, made or contained;
- (2) Permits the publication of any advertisement whether in any newspaper or otherwise, for the sale or supply at a bargain price, of goods or the services that are not intended to be offered for sale or supply at the bargain price, or for a period that is, and in quantities that are, reasonable, having regard to the nature of the market in which the business is carried on, the nature and size of business, and the nature of the advertisement.

Explanation.— For the purposes of CI. (2), “bargaining price” means

- (a) A price that is stated in any advertisement to be a bargain price, by reference to an ordinary price or otherwise, or
- (b) A price that a person who reads, hears or sees the advertisement, would reasonably understand to be a bargain price having regard to the prices at which the product advertised or like products are ordinarily sold.
- (3) Permits—
 - (a) The offering of gifts, prizes or other items with the intention of not providing them as offered or creating impression that something is being given or offered free of charge when it is fully or partly covered by the amount charged in the transaction as a whole;
 - (b) The conduct of any contest, lottery, game of chance or skill, for the purpose of promoting, directly or indirectly, the sale, use or supply of any product or any business interest;

[(3A) withholding from the participants of any scheme offering gifts, prizes or other items free of charge, on its closure the information about final results of the scheme.

Explanation : for the purposes of this sub-clause, the participants of a scheme shall be deemed to have been informed of the final results of the scheme where such results are within a reasonable time published, prominently in the same newspapers in which the scheme was originally advertised.



- (4) Permits the sale or supply of goods intended to be used, or are of kind likely to be used, by consumers, knowing or having reason to believe that the goods do not comply with the standards prescribed by competent authority relating to performance, composition, contents. Design, constructions, finishing or packaging as are necessary to prevent or reduce the risk of injury to the person using the goods;
- (5) Permits the hoarding or destruction of goods, or refuses to sell the goods or to make them available for sale or to provide any service, if such hoarding or destruction or refusal raises or tends to raises or is intended to raise, the cost of those or other similar goods or services.”
- (6) Manufacture of spurious goods or offering such good for sale or adopting deceptive practices in the provision of Services.
- (2) Any reference in this Act to any other Act or provision thereof which is not in force in any area to which this Act applies shall be construed to have reference to the corresponding Act or provision thereof in force in such areas.

3. JURISDICTION

District Forums : have the Jurisdiction to entertain complaints -

If the cost of goods or services and compensation asked for is up to rupees twenty lakh.

State Commission : has the Jurisdiction to entertain complaints,

If the cost of goods or services and compensation asked for is more than rupees twenty lakh , but less than rupees one Crore.

The State Commission also has the jurisdiction to entertain appeal against the orders of any District Forum within the State.

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 :-

- (a) it appears that such District Forum has exercised any power not vested in it by law or
- (b) has failed to exercise a power rightfully vested in it by law, or
- (c) has acted illegally or with material irregularity.

National Commission : has jurisdiction to entertain complaints—

If the cost of goods or services and compensation asked for exceed rupees one crore then the complaint can be filed before the National Commission at New Delhi.

The National Commission besides entertaining the original complaints also has jurisdiction to entertain appeals against the orders of any State Commission; and 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:

- (a) where it appears to it that such Commission has exercised a jurisdiction not vested in it by law, or
- (b) has failed to exercise a jurisdiction so vested, or
- (c) has acted in the exercise of its jurisdiction illegally or with material irregularity.

4. PLACE OF INSTITUTING A CONSUMER COMPLAINT

A complaint shall be instituted in the District Forum/State Commission/National Commission within the local limits of whose jurisdiction—

- (a) The opposite party 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 party(s), 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 District forum/State Commission/National Commission is given, or the opposite party(s) 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.

**5. WHO MAY/CAN FILE COMPLAINTS**

Complaints may be filed with the District Forum/State Commission/National Commission by :-

1. 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.
2. Any recognised consumer association, whether the consumer to whom 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.
3. 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.
4. The Central or the State Government.

Every complaint filed shall be filed along with such amount of fee as may be prescribed.

6. LIMITATION PERIOD FOR FILING OF COMPLAINT

The Period of Limitation prescribed for the filing of complaints before District Forum, the State Commission, or the National Commission is two years from the date on which the cause of action has arisen. However, if the complainant satisfies the District Forum / State Commission, 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.

7. PROCEDURE ON ADMISSION OF COMPLAINT

On admission of a complaint, a copy of the complaint is to be referred to the opposite party within 21 days, directing him to give his version of the case within 30 days. This period may be extended by another 15 days.

Where the opposite party denies or disputes the allegations or omits or fails to take any action to represent his case within the time provided, the dispute will be settled in the following manner :-

I. If the Dispute Relates to 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 manner prescribed 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 other 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.

The District Forum / State Commission may require the complainant to deposit with it such amount as may be specified towards payment of fees to the appropriate laboratory for carrying out the tests. 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 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.

II. If Dispute relates to Goods not requiring testing or analysis or relates to services :

Where the opposite party denies or disputes the allegations contained in the complaint within the time given by the District Forum / State Commission, it 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 ex parte on the basis of evidence tendered by the complainant.

Where during the pendency of any proceeding before the District Forum, it appears to it necessary, it may pass such interim order as is just and proper in the facts and circumstances of the case.



8. POWERS OF THE DISPUTE REDRESSAL AGENCIES

The District Forum, State Commission and the National Commission are vested with the powers of a civil court under the Code of Civil Procedure while trying a suit in respect of the following matters:-

1. The summoning and enforcing attendance of any defendant or witness examining the witness on oath;
2. The discovery and production of any document or other material producible as evidence;
3. The reception of evidence on affidavits;
4. The requisitioning of the report of the concerned analysis or test from the appropriate laboratory or from any other relevant source;
5. Issuing of any commission for the examination of any witness; and
6. Any other matter which may be prescribed.

They also have the power to :-

- (i) to issue remedial orders against the opposite party.
- (ii) to dismiss frivolous and vexatious complaints and to order the complainant to make payment of costs, not exceeding ` 10,000 to the opposite party.

9. RELIEF(S) THAT MAY BE GRANTED UNDER THE ACT

The District Forum / State Commission / National Commission may pass one or more of the following orders to grant relief to the aggrieved consumer :-

- (a) to remove the defect 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;

Provided that the District Forum shall have the power to grant punitive damages in such circumstances as it deems fit.

- (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;
- (i) to cease manufacture of hazardous goods and to desist from offering services which are hazardous in nature;
- (j) 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;
- (k) to issue corrective advertisement to neutralize the effect of misleading advertisement at the cost of the opposite party responsible for issuing such misleading advertisement;
- (l) to provide for adequate costs to parties.

10. APPEALS

(i) Against the orders of District Forums :

Any person aggrieved by an order made by the Forum may prefer an appeal to the State Commission within thirty days from the date of the impugned order

(ii) Against the orders of State Commission :

Similarly, any person aggrieved by any original order of the State Commission may prefer an appeal to the National Commission within thirty days from the date of the impugned order.

**(iii) Against the orders of National Commission :**

Any person aggrieved by any original order of the National Commission may prefer an appeal to the Supreme Court.

The Appellate authority may entertain an appeal after the said period of thirty days if sufficient cause for not filling the appeal within the stipulated period is shown to its satisfaction. The period of 30 days is to be computed from the date of receipt of the order by the parties concerned.

11. REVISION AGAINST THE ORDER OF STATE COMMISSION

Any person aggrieved by any order of the State Commission passed in an appeal against the order of District Forum may file a revision against such an order before the National Commission. The Act does not provide for second appeal and therefore the only remedy is a Revision.

If no appeal is preferred against the order, the said order becomes final.

12. ENFORCEMENT OF ORDERS

1. If an interim order made is not complied with, the District Forum/State Commission/ National Commission may order the property of the person, not complying with such order to be attached.
2. Attachment so made remains operative only for more than three months at the end of which, if the non-compliance continues, the property attached can be sold and out of the proceeds thereof, the Forum, State or National Commission may award such damages as it thinks fit to the complainant and shall pay the balance, if any, to the party entitled thereto.
3. If any amount is due from any person under an order made by a District Forum, State or the National Commission, the person entitled to the amount may make an application to the District Forum, State or the National Commission, who may issue a certificate for the said amount to the Collector of the district and the Collector shall proceed to recover the amount in the same manner as arrears of land revenue.

13. PENALTIES

Failure or omission to comply with any order of the Forum, State Commission or the National Commission by the party against whom such an order is passed is punishable with imprisonment for a term which shall not be less than one month, which may extend to 3 years, or with fine of not less than ` 2,000 & it may be upto ` 10000 or with both.



Study Note – 4

OTHER LAWS

This study note includes

- Limited Liability Partnership Act, 2008
- RTI Act, 2005
- The Competition Act, 2002
- Negotiable Instrument Act, 1881

4.1 LIMITED LIABILITY PARTNERSHIP ACT, 2008

An Act to make provisions for the formation and regulation of limited liability partnerships and for matters connected therewith or incidental thereto.

Short title, extent and commencement.

1. (i) This Act may be called the Limited Liability Partnership Act, 2008.
- (ii) It extends to the whole of India.
- (iii) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint :

Provided that different dates may be appointed for different provisions of this Act and any reference in any such provision to the commencement of this Act shall be construed as a reference to the coming into force of that provision.

Definitions :

2. (A) In this Act, unless the context otherwise requires,—

- (a) “address”, in relation to a partner of a limited liability partnership, means-
 - (i) if an individual, his usual residential address; and
 - (ii) if a body corporate, the address of its registered office;
- (b) “advocate” means an advocate as defined in clause (a) of sub-section (1) of section 2 of the Advocates Act, 1961;
- (c) “Appellate Tribunal” means the National Company Law Appellate Tribunal constituted under sub-section (1) of section 10 of the Companies Act, 1956;
- (d) “body corporate” means a company as defined in section 3 of the Companies Act, 1956 and includes-
 - (i) a limited liability partnership registered under this Act;
 - (ii) a limited liability partnership incorporated outside India; and
 - (iii) a company incorporated outside India,but does not include-
 - (i) a corporation sole;
 - (ii) a co-operative society registered under any law for the time being in force; and
 - (iii) any other body Corporate (not being a company as defined in section 3 of the Companies Act, 1956 or a limited liability partnership as defined in this Act), which the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (e) “business” includes every trade, profession, service and occupation;



- (f) “chartered accountant” means a chartered accountant as defined in clause (b) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;
- (g) “company secretary” means a company secretary as defined in clause (c) of sub-section (1) of section 2 of the Company Secretaries Act, 1980 and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;
- (h) “cost accountant” means a cost accountant as defined in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;
- (i) “Court”, with respect to any offence under this Act, means the Court having jurisdiction as per the provisions of section 77;
- (j) “designated partner” means any partner designated as such pursuant to section 7;
- (k) “entity” means any body corporate and includes, for the purposes of sections 18,46,47,48,49,50,52 and 53, a firm set-up under the Indian Partnership Act, 1932;
- (l) “financial year”, in relation to a limited liability partnerships, means the period from the 1st day of April of a year to the 31st day of March of the following year :

Provided that in the case of a limited liability partnership incorporated after the 30th day of September of a year, the financial year may end on the 31st day of March of the year next following that year;

- (m) “foreign limited liability partnership” means a limited liability partnership formed, incorporated or registered outside India which establishes a place of business within India;
- (n) “limited liability partnership” means a partnership formed and registered under this Act;
- (o) “limited liability partnership agreement” means any written agreement between the partners of the limited liability partnership or between the limited liability partnership and its partners which determines the mutual rights and duties of the partners and their rights and duties in relation to that limited liability partnership;
- (p) “name”, in relation to a partner of a limited liability partnership, means—
 - (i) if an individual, his forename, middle name and surname; and
 - (ii) if a body corporate, its registered name;
- (q) “partner”, in relation to a limited liability partnership, means any person who becomes a partner in the limited liability partnership in accordance with the limited liability partnership agreement;
- (r) “prescribed” means prescribed by rules made under this Act;
- (s) “Registrar” means a Registrar, or an Additional, a Joint, a Deputy or an Assistant Registrar, having the duty of registering companies under the Companies Act, 1956;
- (t) “Schedule” means a Schedule to this Act;
- (u) “Tribunal” means the National Company Law Tribunal constituted under sub-section (1) of section 10FB of the Companies Act, 1956.

(B) Words and expressions used and not defined in this Act but defined in the Companies Act, 1956 shall have the meanings respectively assigned to them in that Act.

NATURE OF LIMITED LIABILITY PARTNERSHIP

Limited liability partnership to be body corporate

3. (1) A limited liability partnership is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners.
- (2) A limited liability partnership shall have perpetual succession.
- (3) Any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.



Non-applicability of the Indian Partnership Act, 1932.

4. Save as otherwise provided, the provisions of the Indian Partnership Act, 1932 shall not apply to a limited liability partnership.

Partners.

5. Any individual or **body corporate** may be a partner in a limited liability partnership:

Provided that an individual shall not be capable of becoming a partner of a limited liability partnership, if—

- (a) he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force;
- (b) he is an undischarged insolvent; or
- (c) he has applied to be adjudicated as an insolvent and his application is pending.

Minimum number of partners.

6. (1) Every limited liability partnership shall have at least two partners.
- (2) If at any time the number of partners of a limited liability partnership is reduced below two and the limited liability partnership carries on business for more than six months while the number is so reduced, the person, who is the only partner of the limited liability partnership during the time that it so carries on business after those six months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the limited liability partnership incurred during that period.

Designated partners.

7. (1) Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India:

Provided that in case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners.

Explanation : For the purposes of this section, the term “resident in India” means a person who has stayed in India for a period of not less than one hundred and eighty-two days during the immediately preceding one year.

- (2) Subject to the provisions of sub-section (1),—
- (i) if the incorporation document—
 - (a) specifies who are to be designated partners, such persons shall be designated partners on incorporation; or
 - (b) states that each of the partners from time to time of limited liability partnership is to be designated partner, every partner shall be a designated partner;
 - (ii) any partner may become a designated partner by and in accordance with the limited liability partnership agreement and a partner may cease to be a designated partner in accordance with limited liability partnership agreement.
- (3) An individual shall not become a designated partner in any limited liability partnership unless he has given his prior consent to act as such to the limited liability partnership in such form and manner as may be prescribed.
- (4) Every limited liability partnership shall file with the registrar the particulars of every individual who has given his consent to act as designated partner in such form and manner as may be prescribed within thirty days of his appointment.
- (5) An individual eligible to be a designated partner shall satisfy such conditions and requirements as may be prescribed.
- (6) Every designated partner of a limited liability partnership shall obtain a Designated Partner Identification Number (DPIN) from the Central Government and the provisions of sections 266A to 266G (both inclusive) of the Companies Act, 1956 shall apply mutatis mutandis for the said purpose.

**Liabilities of designated partners.**

8. Unless expressly provided otherwise in this Act, a designated partner shall be—
- (a) responsible for the doing of all acts, matters and things as are required to be done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement and the like report pursuant to the provisions of this Act and as may be specified in the limited liability partnership agreement; and
 - (b) liable to all penalties imposed on the limited liability partnership for any contravention of those provisions.

Changes in designated partners

9. A limited liability partnership may appoint a designated partner within thirty days of a vacancy arising for any reason and provisions of sub-section (4) and sub-section (5) of section 7 shall apply in respect of such new designated partner:

Provided that if no designated partner is appointed, or if at any time there is only one designated partner, each partner shall be deemed to be a designated partner.

Punishment for contravention of sections 7, 8 and 9.

10. (1) If the limited liability partnership contravenes the provisions of sub-section (1) of section 7, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees.
- (2) If the limited liability partnership contravenes the provisions of sub-section (4) and sub-section (5) of section 7, section 8 or section 9, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

INCORPORATION OF LIMITED LIABILITY PARTNERSHIP AND MATTERS INCIDENTAL THERETO**Incorporation document**

11. (1) For a limited liability partnership to be incorporated,—
- (a) two or more persons associated for carrying on a lawful business with a view to profit shall subscribe their names to an incorporation document;
 - (b) the incorporation document shall be filed in such manner and with such fees, as may be prescribed with the Registrar of the State in which the registered office of the limited liability partnership is to be situated; and
 - (c) there shall be filed along with the incorporation document, a statement in the prescribed form, made by either an advocate, or a Company Secretary or a Chartered Accountant or a Cost Accountant, who is engaged in the formation of the limited liability partnership and by any one who subscribed his name to the incorporation document, that all the requirements of this Act and the rules made thereunder have been complied with, in respect of incorporation and matters precedent and incidental thereto.
- (2) The incorporation document shall—
- (a) be in a form as may be prescribed;
 - (b) state the name of the limited liability partnership;
 - (c) state the proposed business of the limited liability partnership;
 - (d) state the address of the registered office of the limited liability partnership;
 - (e) state the name and address of each of the persons who are to be partners of the limited liability partnership on incorporation;
 - (f) state the name and address of the persons who are to be designated partners of the limited liability partnership on incorporation;
 - (g) contain such other information concerning the proposed limited liability partnership as may be prescribed.
- (3) If a person makes a statement under clause (c) of sub-section (1) which he—
- (a) knows to be false; or
 - (b) does not believe to be true,



shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees.

Incorporation by registration

12. (1) When the requirements imposed by clauses (b) and (c) of sub-section (1) of section 11 have been complied with, the Registrar shall retain the incorporation document and, unless the requirement imposed by clause (a) of that sub-section has not been complied with, he shall, within a period of fourteen days—
- (a) register the incorporation document; and
 - (b) give a certificate that the limited liability partnership is incorporated by the name specified therein.
- (2) The Registrar may accept the statement delivered under clause (c) of sub-section(1) of section 11 as sufficient evidence that the requirement imposed by clause (a) of that sub-section has been complied with.
- (3) The certificate issued under clause (b) of sub-section (1) shall be signed by the Registrar and authenticated by his official seal.
- (4) The certificate shall be conclusive evidence that the limited liability partnership is incorporated by the name specified therein.

Registered office of limited liability partnership and change therein

13. (1) Every limited liability partnership shall have a registered office to which all communications and notices may be addressed and where they shall be received.
- (2) A document may be served on a limited liability partnership or a partner or designated partner thereof by sending it by post under a certificate of posting or by registered post or by any other manner, as may be prescribed, at the registered office and any other address specifically declared by the limited liability partnership for the purpose in such form and manner as may be prescribed.
- (3) A limited liability partnership may change the place of its registered office and file the notice of such change with the Registrar in such form and manner and subject to such conditions as may be prescribed and any such change shall take effect only upon such filing.
- (4) If the limited liability partnership contravenes any provisions of this section, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

Effect of registration

14. On registration, a limited liability partnership shall, by its name, be capable of—
- (a) suing and being sued;
 - (b) acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible;
 - (c) having a common seal, if it decides to have one; and
 - (d) doing and suffering such other acts and things as bodies corporate may lawfully do and suffer.

Name

15. (1) Every limited liability partnership shall have either the words “limited liability partnership” or the acronym “LLP” as the last words of its name.
- (2) No limited liability partnership shall be registered by a name which, in the opinion of the Central Government is —
- (a) undesirable; or
 - (b) identical or too nearly resembles to that of any other partnership firm or limited liability partnership or body corporate or a registered trade mark, or a trade mark which is subject of an application for registration, of any other person under the Trade Marks Act, 1999.



Reservation of name

16. (1) A person may apply in such form and manner and accompanied by such fee as may be prescribed to the Registrar for the reservation of a name set out in the application as—
- (a) the name of a proposed limited liability partnership; or
 - (b) the name to which a limited liability partnership proposes to change its name.
- (2) Upon receipt of an application under sub-section (1) and on payment of the prescribed fee, the Registrar may, if he is satisfied, subject to the rules prescribed by the Central Government in the matter, that the name to be reserved is not one which may be rejected on any ground referred to in sub-section (2) of section 15, reserve the name for a period of three months from the date of intimation by the Registrar.

Change of name of limited liability partner-ship.

17. (1) Notwithstanding anything contained in sections 15 and 16, where the Central Government is satisfied that a limited liability partnership has been registered (whether through inadvertence or otherwise and whether originally or by a change of name) under a name which —
- (a) is a name referred to in sub-section (2) of section 15; or
 - (b) is identical with or too nearly resembles the name of any other limited liability partnership or body corporate or other name as to be likely to be mistaken for it,
- the Central Government may direct such limited liability partnership to change its name, and the limited liability partnership shall comply with the said direction within three months after the date of the direction or such longer period as the Central Government may allow.
- (2) Any limited liability partnership which fails to comply with a direction given under sub-section (1) shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees and the designated partner of such limited liability partnership shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

Application for direction to change name in certain circumstances.

18. (1) Any entity which already has a name similar to the name of a limited liability partnership which has been incorporated subsequently, may apply, in such manner as may be prescribed, to the Registrar to give a direction to any limited liability partnership, on a ground referred to in section 17 to change its name.
- (2) The Registrar shall not consider any application under sub-section (1) to give a direction to a limited liability partnership on the ground referred to in clause (b) of sub-section (1) of section 17 unless the Registrar receives the application within twenty-four months from the date of registration of the limited liability partnership under that name.

Change of registered name.

19. Any limited liability partnership may change its name registered with the Registrar, by filing with him a notice of such change in such form and manner and on payment of such fees as may be prescribed.

Penalty for improper use of words “limited liability partnership” or “LLP”.

20. If any person or persons carry on business under any name or title of which the words “Limited Liability Partnership” or “LLP” or any contraction or imitation thereof is or are the last word or words, that person or each of those persons shall, unless duly incorporated as limited liability partnership, be punishable with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees.

Publication of name and limited liability.

21. (1) Every limited liability partnership shall ensure that its invoices, official correspondence and publications bear the following, namely:-
- (a) the name, address of its registered office and registration number of the limited liability partnership; and
 - (b) a statement that it is registered with limited liability.



- (2) Any limited liability partnership which contravenes the provisions of sub-section (1) shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

PARTNERS AND THEIR RELATIONS

Eligibility to be partners.

22. On the incorporation of a limited liability partnership, the persons who subscribed their names to the incorporation document shall be its partners and any other person may become a partner of the limited liability partnership by and in accordance with the limited liability partnership agreement.

Relationship of partners.

23. (1) Save as otherwise provided by this Act, the mutual rights and duties of the partners of a limited liability partnership, and the mutual rights and duties of a limited liability partnership and its partners, shall be governed by the limited liability partnership agreement between the partners, or between the limited liability partnership and its partners.
- (2) The limited liability partnership agreement and any changes, if any, made therein shall be filed with the Registrar in such form, manner and accompanied by such fees as may be prescribed.
- (3) An agreement in writing made before the incorporation of a limited liability partnership between the persons who subscribe their names to the incorporation document may impose obligations on the limited liability partnership, provided such agreement is ratified by all the partners after the incorporation of the limited liability partnership.
- (4) In the absence of agreement as to any matter, the mutual rights and duties of the partners and the mutual rights and duties of the limited liability partnership and the partners shall be determined by the provisions relating to that matter as are set out in the First Schedule.

Cessation of partnership interest

24. (1) A person may cease to be a partner of a limited liability partnership in accordance with an agreement with the other partners or, in the absence of agreement with the other partners as to cessation of being a partner, by giving a notice in writing of not less than thirty days to the other partners of his intention to resign as partner.
- (2) A person shall cease to be a partner of a limited liability partnership—
- (a) on his death or dissolution of the limited liability partnership; or
- (b) if he is declared to be of unsound mind by a competent court; or
- (c) if he has applied to be adjudged as an insolvent or declared as an insolvent.
- (3) Where a person has ceased to be a partner of a limited liability partnership (hereinafter referred to as “former partner”), the former partner is to be regarded (in relation to any person dealing with the limited liability partnership) as still being a partner of the limited liability partnership unless—
- (a) the person has notice that the former partner has ceased to be a partner of the limited liability partnership; or
- (b) notice that the former partner has ceased to be a partner of the limited liability partnership has been delivered to the Registrar,
- (4) The cessation of a partner from the limited liability partnership does not by itself discharge the partner from any obligation to the limited liability partnership or to the other partners or to any other person which he incurred while being a partner.
- (5) Where a partner of a limited liability partnership ceases to be a partner, unless otherwise provided in the limited liability partnership agreement, the former partner or a person entitled to his share in consequence of the death or insolvency of the former partner, shall be entitled to receive from the limited liability partnership —
- (a) an amount equal to the capital contribution of the former partner actually made to the limited liability partnership; and



- (b) his right to share in the accumulated profits of the limited liability partnership, after the deduction of accumulated losses of the limited liability partnership, determined as at the date the former partner ceased to be a partner.
- (6) A former partner or a person entitled to his share in consequence of the death or insolvency of the former partner shall not have any right to interfere in the management of the limited liability partnership.

Registration of changes in partners

25. (1) Every partner shall inform the limited liability partnership of any change in his name or address within a period of fifteen days of such change.
- (2) A limited liability partnership shall—
 - (a) where a person becomes or ceases to be a partner, file a notice with the Registrar within thirty days from the date he becomes or ceases to be a partner; and
 - (b) where there is any change in the name or address of a partner, file a notice with the Registrar within thirty days of such change.
- (3) A notice filed with the Registrar under sub-section (2)—
 - (a) shall be in such form and accompanied by such fees as may be prescribed;
 - (b) shall be signed by the designated partner of the limited liability partnership and authenticated in a manner as may be prescribed; and
 - (c) if it relates to an incoming partner, shall contain a statement by such partner that he consents to becoming a partner, signed by him and authenticated in the manner as may be prescribed.
- (4) If the limited liability partnership contravenes the provisions of sub-section (2), the limited liability partnership and every designated partner of the limited liability partnership shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.
- (5) If any partner contravenes the provisions of sub-section (1), such partner shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.
- (6) Any person who ceases to be a partner of a limited liability partnership may himself file with the Registrar the notice referred to in sub-section (3) if he has reasonable cause to believe that the limited liability partnership may not file the notice with the Registrar and in case of any such notice filed by a partner, the Registrar shall obtain a confirmation to this effect from the limited liability partnership unless the limited liability partnership has also filed such notice:

Provided that where no confirmation is given by the limited liability partnership within fifteen days, the registrar shall register the notice made by a person ceasing to be a partner under this section.

EXTENT AND LIMITATION OF LIABILITY OF LIMITED LIABILITY PARTNERSHIP AND PARTNERS

Partner as Agent

26. Every partner of a limited liability partnership is, for the purpose of the business of the limited liability partnership, the agent of the limited liability partnership, but not of other partners.

Extent of liability of limited liability partnership

27. (1) A limited liability partnership is not bound by anything done by a partner in a dealing with a person if—
 - (a) the partner in fact has no authority to act for the limited liability partnership in doing a particular act; and
 - (b) the person knows that he has no authority or does not know or believe him to be a partner of the limited liability partnership.
- (2) The limited liability partnership is liable if a partner of a limited liability partnership is liable to any person as a result of a wrongful act or omission on his part in the course of the business of the limited liability partnership or with its authority.



- (3) An obligation of the limited liability partnership whether arising in contract or otherwise, shall be solely the obligation of the limited liability partnership.
- (4) The liabilities of the limited liability partnership shall be met out of the property of the limited liability partnership.

Extent of liability of partner

28. (1) A partner is not personally liable, directly or indirectly for an obligation referred to in sub-section (3) of section 27 solely by reason of being a partner of the limited liability partnership.
- (2) The provisions of sub-section (3) of section 27 and sub-section (1) of this section shall not affect the personal liability of a partner for his own wrongful act or omission, but a partner shall not be personally liable for the wrongful act or omission of any other partner of the limited liability partnership.

Holding out

29. (1) Any person, who by words spoken or written or by conduct, represents himself, or knowingly permits himself to be represented to be a partner in a limited liability partnership is liable to any person who has on the faith of any such representation given credit to the limited liability partnership, whether the person representing himself or represented to be a partner does or does not know that the representation has reached the person so giving credit:

Provided that where any credit is received by the limited liability partnership as a result of such representation, the limited liability partnership shall, without prejudice to the liability of the person so representing himself or represented to be a partner, be liable to the extent of credit received by it or any financial benefit derived thereon.

- (2) Where after a partner's death the business is continued in the same limited liability partnership name, the continued use of that name or of the deceased partner's name as a part thereof shall not of itself make his legal representative or his estate liable for any act of the limited liability partnership done after his death.

Unlimited liability in case of fraud.

30. (1) In the event of an act carried out by a limited liability partnership, or any of its partners, with intent to defraud creditors of the limited liability partnership or any other person, or for any fraudulent purpose, the liability of the limited liability partnership and partners who acted with intent to defraud creditors or for any fraudulent purpose shall be unlimited for all or any of the debts or other liabilities of the limited liability partnership;

Provided that in case any such act is carried out by a partner, the limited liability partnership is liable to the same extent as the partner unless it is established by the limited liability partnership that such act was without the knowledge or the authority of the limited liability partnership.

- (2) Where any business is carried on with such intent or for such purpose as mentioned in sub-section (1), every person who was knowingly a party to the carrying on of the business in the manner aforesaid shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees.
- (3) Where a limited liability partnership or any partner or designated partner or employee of such limited liability partnership has conducted the affairs of the limited liability partnership in a fraudulent manner, then without prejudice to any criminal proceedings which may arise under any law for the time being in force, the limited liability partnership and any such partner or designated partner or employee shall be liable to pay compensation to any person who has suffered any loss or damage by reason of such conduct :

Provided that such limited liability partnership shall not be liable if any such partner or designated partner or employee has acted fraudulently without knowledge of the limited liability partnership.

Whistle blowing

31. (1) The Court or Tribunal may reduce or waive any penalty leviable against any partner or employee of a limited liability partnership, if it is satisfied that—



- (a) such partner or employee of a limited liability partnership has provided useful information during investigation of such limited liability partnership; or
 - (b) when any information given by any partner or employee (whether or not during investigation) leads to limited liability partnership or any partner or employee of such limited liability partnership being convicted under this Act or any other Act.
- (2) No partner or employee of any limited liability partnership may be discharged, demoted, suspended, threatened, harassed or in any other manner discriminated against the terms and conditions of his limited liability partnership or employment merely because of his providing information or causing information to be provided pursuant to sub-section (1).

CONTRIBUTIONS

Form of contribution

32. (1) A contribution of a partner may consist of tangible, movable or immovable or intangible property or other benefit to the limited liability partnership, including money, promissory notes, other agreements to contribute cash or property, and contracts for services performed or to be performed.
- (2) The monetary value of contribution of each partner shall be accounted for and disclosed in the accounts of the limited liability partnership in the manner as may be prescribed.

Obligation to contribute

33. (1) The obligation of a partner to contribute money or other property or other benefit or to perform services for a limited liability partnership shall be as per the limited liability partnership agreement.
- (2) A creditor of a limited liability partnership, which extends credit or otherwise acts in reliance on an obligation described in that agreement, without notice of any compromise between partners, may enforce the original obligation against such partner.

FINANCIAL DISCLOSURES

Maintenance of books of account, other records and audit etc.

34. (1) The limited liability partnership shall maintain such proper books of account as may be prescribed relating to its affairs for each year of its existence on cash basis or accrual basis and according to double entry system of accounting and shall maintain the same at its registered office for such period as may be prescribed.
- (2) Every limited liability partnership shall, within a period of six months from the end of each financial year, prepare a Statement of Account and Solvency for the said financial year as at the last day of the said financial year in such form as may be prescribed, and such statement shall be signed by the designated partners of the limited liability partnership.
- (3) Every limited liability partnership shall file within the prescribed time, the Statement of Account and Solvency prepared pursuant to sub-section (2) with the Registrar every year in such form and manner and accompanied by such fees as may be prescribed.
- (4) The accounts of limited liability partnerships shall be audited in accordance with such rules as may be prescribed:
- Provided that the Central Government may, by notification in the Official Gazette, exempt any class or classes of limited liability partnerships from the requirements of this sub-section.
- (5) Any limited liability partnership which fails to comply with the provisions of this section shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every designated partner of such limited liability partnership shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

Annual Return

35. (1) Every limited liability partnership shall file an annual return duly authenticated with the Registrar within sixty days of closure of its financial year in such form and manner and accompanied by such fee as may be prescribed.



- (2) Any limited liability partnership which fails to comply with the provisions of this section shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees.
- (3) If the limited liability partnership contravenes the provisions of this section, the designated partner of such limited liability partnership shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

Inspection of documents kept by Registrar.

36. The incorporation document, names of partners and changes, if any, made therein, Statement of Account and Solvency and annual return filed by each limited liability partnership with the Registrar shall be available for inspection by any person in such manner and on payment of such fee as may be prescribed.

Penalty for false statement.

37. If in any return, statement or other document required by or for the purposes of any of the provisions of this Act, any person makes a statement—
 - (a) which is false in any material particular, knowing it to be false; or
 - (b) which omits any material fact knowing it to be material,he shall, save as otherwise expressly provided in this Act, be punishable with imprisonment for a term which may extend to two years, and shall also be liable to fine which may extend to five lakh rupees but which shall not be less than one lakh rupees.

Power of Registrar to obtain information.

38. (1) In order to obtain such information as the Registrar may consider necessary for the purposes of carrying out the provisions of this Act, the Registrar may require any person including any present or former partner or designated partner or employee of a limited liability partnership to answer any question or make any declaration or supply any details or particulars in writing to him within a reasonable period.
- (2) In case any person referred to in sub-section (1) does not answer such question or make such declaration or supply such details or particulars asked for by the Registrar within a reasonable time or time given by the Registrar or when the Registrar is not satisfied with the reply or declaration or details or particulars provided by such person, the Registrar shall have power to summon that person to appear before him or an inspector or any other public officer whom the Registrar may designate, to answer any such question or make such declaration or supply such details, as the case may be.
- (3) Any person who, without lawful excuse, fails to comply with any summons or requisition of the Registrar under this section shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

Compounding of offences

39. The Central Government may compound any offence under this Act which is punishable with fine only, by collecting from a person reasonably suspected of having committed the offence, a sum which may extend to the amount of the maximum fine prescribed for the offence.

Destruction of old records.

40. The Registrar may destroy any document filed or registered with him in physical form or in electronic form in accordance with such rules as may be prescribed.

Enforcement of duty to make returns, etc.

41. (1) If any limited liability partnership is in default in complying with—
 - (a) any provisions of this Act or of any other law which requires the filing in any manner with the Registrar of any return, account or other document or the giving of notice to him of any matter; or
 - (b) any request of the Registrar to amend or complete and resubmit any document or to submit a fresh document,



and fails to make good the default within fourteen days after the service on the limited liability partnership of a notice requiring it to be done, the Tribunal may, on application by the Registrar, make an order directing that limited liability partnership or its designated partners or its partners to make good the default within such time as specified in the order.

- (2) Any such order may provide that all the costs of and incidental to the applications shall be borne by that limited liability partnership.
- (3) Nothing in this section shall limit the operation of any other provision of this Act or any other law imposing penalties in respect of any default referred to in this section on that limited liability partnership.

ASSIGNMENT AND TRANSFER OF PARTNERSHIP RIGHTS

Partner's transferable interest.

42. (1) The rights of a partner to a share of the profits and losses of the limited liability partnership and to receive distributions in accordance with the limited liability partnership agreement are transferable either wholly or in part.
- (2) The transfer of any right by any partner pursuant to sub-section (1) does not by itself cause the disassociation of the partner or a dissolution and winding up of the limited liability partnership.
- (3) The transfer of right pursuant to this section does not, by itself, entitle the transferee or assignee to participate in the management or conduct of the activities of the limited liability partnership, or access information concerning the transactions of the limited liability partnership.

INVESTIGATION

Investigating of the affairs of limited liability partnership

43. (1) The Central Government shall appoint one or more competent persons as inspectors to investigate the affairs of a limited liability partnership and to report thereon in such manner as it may direct if—
 - (a) the Tribunal, either suo motu, or on an application received from not less than one-fifth of the total number of partners of limited liability partnership, by order, declares that the affairs of the limited liability partnership ought to be investigated; or
 - (b) any Court, by order, declares that the affairs of a limited liability partnership ought to be investigated.
- (2) The Central Government may appoint one or more competent persons as inspectors to investigate the affairs of a limited liability partnership and to report on them in such manner as it may direct.
- (3) The appointment of inspectors pursuant to sub-section (2) may be made,—
 - (a) if not less than one-fifth of the total number of partners of the limited liability partnership make an application along with supporting evidence and security amount as may be prescribed; or
 - (b) if the limited liability partnership makes an application that the affairs of the limited liability partnership ought to be investigated; or
 - (c) if, in the opinion of the Central Government, there are circumstances suggesting—
 - (i) that the business of the limited liability partnership is being or has been conducted with an intent to defraud its creditors, partners or any other person, or otherwise for a fraudulent or unlawful purpose, or in a manner oppressive or unfairly prejudicial to some or any of its partners, or that the limited liability partnership was formed for any fraudulent or unlawful purpose; or
 - (ii) that the affairs of the limited liability partnership are not being conducted in accordance with the provisions of this Act; or
 - (iii) that, on receipt of a report of the Registrar or any other investigating or regulatory agency, there are sufficient reasons that the affairs of the limited liability partnership ought to be investigated.

Application by partners for investigation.

44. An application by partners of the limited liability partnership under clause (a) of sub-section (1) of section 43 shall be supported by such evidence as the Tribunal may require for the purpose of showing that the applicants have good reason for requiring the investigation and the Central Government may, before appointing an inspector, require the applicants to give security, of such amount as may be prescribed, for payment of costs of the investigation.



Firm, body corporate or association not to be appointed as inspector

45. No firm, body corporate or other association shall be appointed as an inspector.

Power of inspectors to carry out investigation into affairs of related entities, etc.

46. (1) If an inspector appointed by the Central Government to investigate the affairs of a limited liability partnership thinks it necessary for the purposes of his investigation to investigate also the affairs of an entity which has been associated in the past or is presently associated with the limited liability partnership or any present or former partner or designated partner of the limited liability partnership, the inspector shall have the power to do so and shall report on the affairs of the other entity or partner or designated partner, so far as he thinks that the results of his investigation thereof are relevant to the investigation of the affairs of the limited liability partnership.
- (2) In the case of any entity or partner or designated partner referred to in sub-section (1), the inspector shall not exercise his power of investigating into, and reporting on, its or his affairs without first having obtained the prior approval of the Central Government thereto:
- Provided that before according approval under this sub-section, the Central Government shall give the entity or partner or designated partner a reasonable opportunity to show cause why such approval should not be accorded.

Production of documents and evidence

47. (1) It shall be the duty of the designated partner and partners of the limited liability partnership—
- (a) to preserve and to produce before an inspector or any person authorised by him in this behalf with the previous approval of the Central Government, all books and papers of, or relating to, the limited liability partnership or, as the case may be, the other entity, which are in their custody or power; and
 - (b) otherwise to give to the inspector all assistance in connection with the investigation which they are reasonably able to give.
- (2) The inspector may, with the previous approval of the Central Government, require any entity other than an entity referred to in sub section (1) to furnish such information to, or produce such books and papers before him or any person authorised by him in this behalf, with the previous approval of that Government, as he may consider necessary, if the furnishing of such information or the production of such books and papers is relevant or necessary for the purposes of his investigation.
- (3) The inspector may keep in his custody any books and papers produced under sub- section (1) or sub-section (2) for thirty days and thereafter shall return the same to the limited liability partnership, other entity or individual by whom or on whose behalf the books and papers are produced:
- Provided that the inspector may call for the books and papers if they are needed again:
- Provided further that if certified copies of the books and papers produced under sub-section (2) are furnished to the inspector, he shall return those books and papers to the entity or person concerned.
- (4) An inspector may examine on oath—
- (a) any of the persons referred to in sub-section (1);
 - (b) with the previous approval of the Central Government, any other person in relation to the affairs of the limited liability partnership or any other entity, as the case may be; and
 - (c) may administer an oath accordingly and for that purpose may require any of those persons to appear before him personally.
- (5) If any person fails without reasonable cause or refuses—
- (a) to produce before an inspector or any person authorised by him in this behalf with the previous approval of the Central Government any book or paper which it is his duty under sub-section (1) or sub-section (2) to produce ; or
 - (b) to furnish any information which it is his duty under sub section (2) to furnish; or
 - (c) to appear before the inspector personally when required to do so under sub- section (4) or to answer any question which is put to him by the inspector in pursuance of that sub-section; or
 - (d) to sign the notes of any examination,



he shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees and with a further fine which shall not be less than fifty rupees but which may extend to five hundred rupees for every day after the first day after which the default continues.

- (6) The notes of any examination under sub-section (4) shall be taken down in writing and signed by the person whose examination was made on oath and a copy of such notes shall be given to the person so examined on oath and thereafter be used as an evidence by the inspector.

Seizure of documents by inspector.

48. (1) Where in the course of investigation, the inspector has reasonable ground to believe that the books and papers of, or relating to, the limited liability partnership or other entity or partner or designated partner of such limited liability partnership may be destroyed, mutilated, altered, falsified or secreted, the inspector may make an application to the Judicial Magistrate of the first class, or, as the case may be, the Metropolitan Magistrate, having jurisdiction, for an order for the seizure of such books and papers.
- (2) After considering the application and hearing the inspector, if necessary, the Magistrate may, by order, authorise the inspector —
- (a) to enter, with such assistance, as may be required, the place or places where such books and papers are kept;
 - (b) to search that place or those places in the manner specified in the order; and
 - (c) to seize books and papers which the inspector considers it necessary for the purposes of his investigation.
- (3) The inspector shall keep in his custody the books and papers seized under this section for such period not later than the conclusion of the investigation as he considers necessary and thereafter shall return the same to the concerned entity or person from whose custody or power they were seized and inform the Magistrate of such return:
- Provided that the books and papers shall not be kept seized for a continuous period of more than six months:
- Provided further that the inspector may, before returning such books and papers as aforesaid, place identification marks on them or any part thereof.
- (4) Save as otherwise provided in this section, 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 or seizures made under that Code.

Inspector's report

49. (1) The inspectors may, and if so directed by the Central Government, shall make interim reports to that Government, and on the conclusion of the investigation, shall make a final report to the Central Government and any such report shall be written or printed, as the Central Government may direct.
- (2) The Central Government-
- (a) shall forward a copy of any report (other than an interim report) made by the inspectors to the limited liability partnership at its registered office, and also to any other entity or person dealt with or related to the report; and
 - (b) may, if it thinks fit, furnish a copy thereof, on request and on payment of the prescribed fee, to any person or entity related to or affected by the report.

Prosecution

50. If, from the report under section 49, it appears to the Central Government that any person in relation to the limited liability partnership or in relation to any other entity whose affairs have been investigated, has been guilty of any offence for which he is liable, the Central Government may prosecute such person for the offence; and it shall be the duty of all partners, designated partners and other employees and agents of the limited liability partnership or other entity, as the case may be, to give the Central Government all assistance in connection with the prosecution which they are reasonably able to give.



Application for winding up of limited liability partnership

51. If any such limited liability partnership is liable to be wound up under this Act or any other law for the time being in force, and it appears to the Central Government from any such report under section 49 that it is expedient to do so by reason of any such circumstances as are referred to in sub-clause (i) or sub-clause (ii) of clause (c) of sub-section (3) of section 43, the Central Government may, unless the limited liability partnership is already being wound up by the Tribunal, cause to be presented to the Tribunal by any person authorised by the Central Government in this behalf, a petition for the winding up of the limited liability partnership on the ground that it is just and equitable that it should be wound up.

Proceedings for recovery of damages or property

52. If, from any report under section 49, it appears to the Central Government that proceedings ought, in the public interest, to be brought by the limited liability partnership or any entity whose affairs have been investigated,—
- (a) for the recovery of damages in respect of any fraud, misfeasance or other misconduct in connection with the promotion or formation, or the management of the affairs, of such limited liability partnership or such other entity; or
 - (b) for the recovery of any property of such limited liability partnership or such other entity, which has been misapplied or wrongfully retained,
- the Central Government may itself bring proceedings for that purpose.

Expenses of Investigation

53. (1) The expenses of and incidental to an investigation by an inspector appointed by the Central Government under this Act shall be defrayed in the first instance by the Central Government; but the following persons shall, to the extent mentioned below, be liable to reimburse the Central Government in respect of such expenses, namely:—
- (a) any person who is convicted on a prosecution, or who is ordered to pay damages or restore any property in proceedings brought by virtue of section 52, may, in the same proceedings, be ordered to pay the said expenses to such extent as may be specified by the court convicting such person, or ordering him to pay such damages or restore such property, as the case may be;
 - (b) any entity in whose name proceedings are brought as aforesaid shall be liable, to the extent of the amount or value of any sums or property recovered by it as a result of the proceedings; and
 - (c) unless, as a result of the investigation, a prosecution is instituted in pursuance of section 50,—
 - (i) any entity, a partner or designated partner or any other person dealt with by the report of the inspector shall be liable to reimburse the Central Government in respect of the whole of the expenses, unless and except in so far as, the Central Government otherwise directs; and
 - (ii) the applicants for the investigation, where the inspector was appointed in pursuance of the provisions of clause (a) of sub-section (1) of section 43, shall be liable to such extent, if any, as the Central Government may direct.
- (2) Any amount for which a limited liability partnership or other entity is liable by virtue of clause (b) of sub-section (1) shall be a first charge on the sums or property mentioned in that clause.
- (3) The amount of expenses in respect of which any limited liability partnership, other entity, a partner or designated partner or any other person is liable under sub-clause (i) of clause (c) of sub-section (1) to reimburse the Central Government shall be recoverable as arrears of land revenue.
- (4) For the purposes of this section, any costs or expenses incurred by the Central Government or in connection with the proceedings brought by virtue of section 52 shall be treated as expenses of the investigation giving rise to the proceedings.

Inspector's report to be evidence

54. A copy of any report of any inspector or inspectors appointed under the provision of this Act, authenticated in such manner, if any, as may be prescribed, shall be admissible in any legal proceeding as evidence in relation to any matter contained in the report.



CONVERSION TO LIMITED LIABILITY PARTNERSHIP

Conversion from firm into limited liability partnership.

55. A firm may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Second Schedule.

Conversion from private company into limited liability partnership.

56. A private company may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Third Schedule.

Conversion from unlisted public company into limited liability partnership

57. An unlisted public company may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Fourth Schedule

Registration and effect of conversion

58. (1) The Registrar, on satisfying that a firm, private company or an unlisted public company, as the case may be, has complied with the provisions of the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be, shall, subject to the provisions of this Act and the rules made thereunder, register the documents submitted under such Schedule and issue a certificate of registration in such form as the Registrar may determine stating that the limited liability partnership is, on and from the date specified in the certificate, registered under this Act:

Provided that the limited liability partnership shall, within fifteen days of the date of registration, inform the concerned Registrar of Firms or Registrar of Companies, as the case may be, with which it was registered under the provisions of the Indian Partnership Act, 1932 or the Companies Act, 1956, as the case may be, about the conversion and of the particulars of the limited liability partnership in such form and manner as may be prescribed.

- (2) Upon such conversion, the partners of the firm, the shareholders of private company or unlisted public company, as the case may be, the limited liability partnership to which such firm or such company has converted, and the partners of the limited liability partnership shall be bound by the provisions of the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be, applicable to them.
- (3) Upon such conversion, on and from the date of certificate of registration, the effects of the conversion shall be such as specified in the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be.
- (4) Notwithstanding anything contained in any other law for the time being in force, on and from the date of registration specified in the certificate of registration issued under the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be,—
 - (a) there shall be a limited liability partnership by the name specified in the certificate of registration registered under this Act;
 - (b) all tangible (movable or immovable) and intangible property vested in the firm or the company, as the case may be, all assets, interests, rights, privileges, liabilities, obligations relating to the firm or the company, as the case may be, and the whole of the undertaking of the firm or the company, as the case may be, shall be transferred to and shall vest in the limited liability partnership without further assurance, act or deed; and
 - (c) The firm or the company, as the case may be, shall be deemed to be dissolved and removed from the records of the Registrar of Firms or Registrar of Companies, as the case may be.

FOREIGN LIMITED LIABILITY PARTNERSHIP

Foreign limited liability partnerships

59. The Central Government may make rules for provisions in relation to establishment of place of business by foreign limited liability partnerships within India and carrying on their business therein by applying or incorporating, with such modifications, as appear appropriate, the provisions of the Companies Act, 1956 or such regulatory mechanism with such composition as may be prescribed.



COMPROMISE, ARRANGEMENT OR RECONSTRUCTION OF LIMITED LIABILITY PARTNERSHIP

Compromise, arrangement or reconstruction of limited liability partnerships

60. (1) Where a compromise or arrangement is proposed-

- (a) between a limited liability partnership and its creditors; or
- (b) between a limited liability partnership and its partners,

the Tribunal may, on the application of the limited liability partnership or of any creditor or partner of the limited liability partnership, or, in the case of a limited liability partnership which is being wound up, of the liquidator, order a meeting of the creditors or of the partners, as the case may be, to be called, held and conducted in such manner as may be. Prescribed or as the Tribunal directs.

- (2) If a majority representing three-fourths in value of the creditors, or partners, as the case may be, at the meeting, agree to any compromise or arrangement, the compromise or arrangement shall, if sanctioned by the Tribunal, by order be binding on all the creditors or all the partners, as the case may be, and also on the limited liability partnership, or in the case of a limited liability partnership which is being wound up, on the liquidator and contributories of the limited liability partnership:

Provided that no order sanctioning any compromise or arrangement shall be made by the Tribunal unless the Tribunal is satisfied that the limited liability partnership or any other person by whom an application has been made under sub-section (1) has disclosed to the Tribunal, by affidavit or otherwise, all material facts relating to the limited liability partnership, including the latest financial position of the limited liability partnership and the pendency of any investigation proceedings in relation to the limited liability partnership.

- (3) An order made by the Tribunal under sub-section (2) shall be filed by the limited liability partnership with the Registrar within thirty days after making such an order and shall have effect only after it is so filed.
- (4) If default is made in complying with sub-section (3), the limited liability partnership, and every designated partner of the limited liability partnership shall be punishable with fine which may extend to one lakh rupees.
- (5) The Tribunal may, at any time after an application has been made to it under this section, stay the commencement or continuation of any suit or proceeding against the limited liability partnership on such terms as the Tribunal thinks fit, until the application is finally disposed of.

Power of Tribunal to enforce compromise or arrangement

61. (1) Where the Tribunal makes an order under section 60 sanctioning a compromise or an arrangement in respect of a limited liability partnership, it

- (a) shall have power to supervise the carrying out of the compromise or an arrangement; and
- (b) may, at the time of making such order or at any time thereafter, give such directions in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the proper working of the compromise or arrangement.

- (2) If the Tribunal aforesaid is satisfied that a compromise or an arrangement sanctioned under section 60 cannot be worked satisfactorily with or without modifications, it may, either on its own motion or on the application of any person interested in the affairs of the limited liability partnership, make an order for winding up the limited liability partnership, and such an order shall be deemed to be an order made under section 64 of this Act.

Provision for facilitating reconstruction or amalgamation of limited liability partnership

62. (1) Where an application is made to the Tribunal under section 60 for sanctioning of a compromise or arrangement proposed between a limited liability partnership and any such persons as are mentioned in that section, and it is shown to the Tribunal that—

- (a) compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of any limited liability partnership or limited liability partnerships, or the amalgamation of any two or more limited liability partnerships; and
- (b) under the scheme the whole or any part of the undertaking, property or liabilities of any limited liability partnership concerned in the scheme (in this section referred to as a “transferor limited



liability partnership”) is to be transferred to another limited liability partnership (in this section referred to as the “transferee limited liability partnership”),

the Tribunal may, either by the order sanctioning the compromise or arrangement or by a subsequent order, make provisions for all or any of the following matters, namely:—

- (i) the transfer to the transferee limited liability partnership of the whole or any part of the undertaking, property or liabilities of any transferor limited liability;
- (ii) the continuation by or against the transferee limited liability partnership of any legal proceedings pending by or against any transferor limited liability partnership;
- (iii) the dissolution, without winding up, of any transferor limited liability partnership;
- (iv) the provision *to* be made for any person who, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement; and
- (v) such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction or amalgamation shall be fully and effectively carried out:

Provided that no compromise or arrangement proposed for the purposes of, or *In* connection with, a scheme for the amalgamation of a limited liability partnership, which is being wound up, with any other limited liability partnership or limited liability partnerships, shall be sanctioned by the Tribunal unless the Tribunal has received a report from the Registrar that the affairs of the limited liability partnership have not been conducted in a manner prejudicial to the interests of its partners or to public interest:

Provided further that no order for the dissolution of any transferor limited liability partnership under clause (iii) shall be made by the Tribunal unless the Official Liquidator has, on scrutiny of the books and papers of the limited liability partnership, made a report to the Tribunal that the affairs of the limited liability partnership have not been conducted in a manner prejudicial to the interests of its partners or to public interest.

- (2) Where an order under this section provides for the transfer of any property or liabilities, then, by virtue of the order, that property shall be transferred to and vest in, and those liabilities shall be transferred to and become the liabilities of, the transferee limited liability partnership; and in the case of any property, if the order so directs, freed from any charge which is, by virtue of the compromise or arrangement, to cease to have effect.
- (3) Within thirty days after the making of an order under this section, every limited liability partnership in relation to which the order is made shall cause a certified copy thereof to be filed with the Registrar for registration.
- (4) If default is made in complying with the provisions of sub-section (3), the limited liability partnership, every designated partner of the limited liability partnership shall be punishable with fine which may extend to fifty thousand rupees.

Explanation. In this section “property” includes property, rights and powers of every description; and “liabilities” includes duties of every description.

WINDING UP AND DISSOLUTION

Winding up and dissolution

63. The winding up of a limited liability partnership may be either voluntary or by Tribunal and limited liability partnership, so wound up may be dissolved.

Circumstance in which Limited liability Partnership may be wound up by Tribunal

64. A limited liability partnership may be wound up by the Tribunal,—

- (a) the limited liability partnership decides that limited liability partnership be wound up by the Tribunal;
- (b) If , for a period of more than six month ,the number of partners of the limited liability partnership is reduced below two;
- (c) if the limited liability partnership is unable to pay its debts;
- (d) if the limited liability partnership has acted against the interests of the sovereignty and integrity of India, the security of the State or public order;



- (e) if the limited liability partnership has made a default in filing with the Registrar the Statement of Account and Solvency or annual return for any five consecutive financial years; or
- (f) if the Tribunal is of the opinion that it is just and equitable that the limited liability partnership be wound up

Rules for winding up and dissolution

65. The Central Government may make rules for the provisions in relation to winding up and dissolution of limited liability partnerships.

MISCELLANEOUS

Business transaction of partner with Limited liability partnership

66. A partner may lend money to and transact other business with the limited liability partnership and has the same rights and obligations with respect to the loan or other transactions as a person who is not a partner.

Application of the Provision of the Companies Act

67. (1) The Central Government may, by notification in the Official Gazette, direct Application that any of the provisions of the Companies Act, 1956 specified in the notification-
- (a) shall apply to any limited liability partnership; or
 - (b) shall apply to any limited liability partnership with such exception modification and adaptation, as may be specified, in the notification.
- (2) A copy of every notification proposed to be issued under sub-section (1) shall be laid in draft 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 disapproving the issue of the notification or both Houses agree in making any modification in the notification, 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.

Electronic filing of document.

68. (1) Any document required to be filed, recorded or registered under this Act may be filed, recorded or registered in such manner and subject to such conditions as may be prescribed.
- (2) A copy of or an extract from any document electronically filed with or submitted to the Registrar which is supplied or issued by the Registrar and certified through affixing digital signature as per the Information Technology Act, 2000 to be a true copy of or extract from such document shall, in any proceedings, be admissible in evidence as of equal validity with the original document.
- (3) Any information supplied by the Registrar that is certified by the Registrar through affixing digital signature to be a true extract from any document filed with or submitted to the Registrar shall, in any proceedings, be admissible in evidence and be presumed, unless evidence to the contrary is adduced, to be a true extract from such document.

Payment of additional.

69. Any document or return required to be filed or registered under this Act with the Registrar, if, is not filed or registered in time provided therein, may be filed or registered after that time upto a period of three hundred days from the date within which it should have been filed, on payment of additional fee of one hundred rupees for every day of such delay in addition to any fee as is payable for filing of such document or return:

Provided that such document or return may, without prejudice to any other action or liability under this Act, also be filed after such period of three hundred days on payment of fee and additional fee specified in this section.

Enhanced punishment

70. In case a limited liability partnership or any partner or designated partner of such limited liability partnership commits any offence, the limited liability partnership or any partner or designated partner shall, for the



second or subsequent offence, be punishable with imprisonment as provided, but in case of offences for which fine is prescribed either along with or exclusive of imprisonment, with fine which shall be twice the amount of fine for such offence.

Application of other laws not barred.

71. The provisions of this Act shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force,

Jurisdiction of Tribunal and Appellate Tribunal

72. (1) The Tribunal shall exercise such powers and perform such functions as are, or may be, conferred on it by or under this Act or any other law for the time being in force.
- (2) Any person aggrieved by an order or decision of Tribunal may prefer an appeal to the Appellate Tribunal and the provisions of sections 10FQ, 10FZA, 10G, 10GD, 10GE and 10GF of the Companies Act, 1956 shall be applicable in respect of such appeal.

Penalty on non-compliance of any order passed by Tribunal

73. Whoever fails to comply with any order made by the Tribunal under any provision of this Act shall be punishable with imprisonment which may extend to six months and shall also be liable to a fine which shall not be less than fifty thousand rupees.

General penalties.

74. Any person guilty of an offence under this Act for which no punishment is expressly provided shall be liable to a fine which may extend to five lakh rupees but which shall not be less than five thousand rupees and with a further fine which may extend to fifty rupees for every day after the first day after which the default continues.

Power of registrar to strike defunct limited liability partnership off register

75. Where the Registrar has reasonable cause to believe that a limited liability partnership is not carrying on business or its operation, in accordance with the provisions of this Act, the name of limited liability partnership may be struck off the register of limited liability partnerships in such manner as may be prescribed:
- Provided that the Registrar shall, before striking off the name of any limited liability partnership under this section, give such limited liability partnership a reasonable opportunity of being heard.

Offence of limited liability partnerships

76. Where an offence under this Act committed by a limited liability partnership is proved —
- (a) to have been committed with the consent or connivance of a partner or partners or designated partner or designated partners of the limited liability partnership; or
 - (b) to be attributable to any neglect on the part of the partner or partners or designated partner or designated partners of that limited liability partnership, the partner or partners or designated partner or designated partners of the limited liability partnership, as the case may be, as well as that limited liability partnership shall be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

Jurisdiction of the court

77. Notwithstanding any provision to the contrary in any Act for the time being in force, the Judicial Magistrate of the first class or, as the case may be, the Metropolitan Magistrate shall have jurisdiction or try any offence under this Act and shall have power to impose punishment in respect of said offence.

Power to alter Schedule.

78. (1) The Central Government may by notification in the Official Gazette, alter any of the provisions contained in any of the Schedules to this Act.
- (2) Any alteration notified under sub-section (1) shall have effect as if enacted in the Act and shall come into force on the date of the notification, unless the notification otherwise directs.
- (3) Every alteration made by the Central Government under sub-section (1) shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days 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 alteration, or both Houses agree that the alteration should not be made, the alteration 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 in pursuance of that alteration.

79. (1) The Central Government may, by notification in the Official Gazette, make rules for carrying out the provisions of this Act.
- (2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely :-
- (a) form and manner of prior consent to be given by designated partner under sub-section (3) of section 7;
 - (b) the form and manner of particulars of every individual agreeing to act as designated partner of limited liability partnership under sub-section (4) of section 7;
 - (c) the conditions and requirements relating to the eligibility of an individual to become a designated partner under sub-section (5) of section 7;
 - (d) the manner of filing the incorporation document and payment of fees payable thereof under clause (b) of sub-section (l) of section 11;
 - (e) the form of statement to be filed under clause (c) of sub-section (l) of section 11;
 - (f) the form of incorporation document under clause (a) of sub-section (2) of section 11;
 - (g) the information to be contained in the incorporation document concerning the proposed limited liability partnership under clause (g) of sub-section (2) of section 11;
 - (h) the manner of serving the documents on a limited liability partnership or a partner or a designated partner and the form and manner in which any other address may be declared by the limited liability partnership under sub-section (2) of section 13;
 - (i) the form and manner of notice to the Registrar and the conditions in respect of change of registered office under sub-section (3) of section 13;
 - (j) the form and manner of application and amount of fee payable to the Registrar under sub-section (l) of section 16;
 - (k) the manner in which names will be reserved by the Registrar under sub-section (2) of section 16;
 - (l) the manner in which an application may be made by an entity under sub-section (1) section 18;
 - (m) the form and manner of notice of change of name of limited liability partnership and the amount of fee payable under section 19;
 - (n) the form and manner of the limited partnership agreement and the changes made therein and the amount of fee payable under sub-section (2) of section 23;
 - (o) the form of notice, the amount of fee payable and the manner of authentication of the statement under clauses (a), (b) and (c) of sub-section (3) of section 25;
 - (p) the manner of accounting and disclosure of monetary value of contribution of a partner under sub-section (2) of section 32;
 - (q) the books of account and the period of their maintenance under sub-section (1) of section 34;
 - (r) the form of Statement of Account and Solvency under sub-section (2) of section 34;
 - (s) the form, manner, fee and time of filing of Statement of Account and Solvency under sub-section (3) of section 34;
 - (t) the audit of accounts of a limited liability partnership under sub-section (4) of section 34;
 - (u) the form and manner of annual return and fee payable under sub-section (1) of section 35;
 - (v) the manner and amount of fee payable for inspection of incorporation documents, names of partners and changes made therein, Statement of Account and Solvency and annual return under section 36;
 - (w) the destruction of documents by Registrar in any form under section 40;



- (x) the amount required as security under clause (a) of sub-section (3) of section 43;
 - (y) the amount of security to be given under section 44;
 - (z) the fee payable for furnishing a copy under clause (b) of sub-section (2) of section 49;
 - (za) the manner of authentication of report of inspector under section 54;
 - (zb) the form and manner of particulars about conversion under the proviso to sub-section (1) of section 58;
 - (zc) in relation to establishment of place of business and carrying on business in India by foreign limited liability partnerships and regulatory mechanism and composition under section 59;
 - (zd) the manner of calling, holding and conducting meeting under sub-section (1) of section 60;
 - (ze) in relation to winding up and dissolution of limited liability partnerships under section 65;
 - (zf) the manner and conditions for filing document electronically under sub-section (1) of section 68;
 - (zg) the manner for striking off the names of limited partnership from the register under section 75;
 - (zh) the form and manner of statement containing particulars and amount of fee payable under sub-paragraph (a) of paragraph 4 of the Second Schedule;
 - (zi) the form and manner of particulars about conversion under the proviso to paragraph 5 of the Second Schedule;
 - (zj) the form and manner of the statement and the amount of fee payable under sub-paragraph (a) of paragraph 3 of the Third Schedule;
 - (zk) the form and manner of particulars about conversion under the proviso to paragraph 4 of the Third Schedule;
 - (zl) the form and manner of the statement and amount of fee payable under sub-paragraph 4 of the Third Schedule;
 - (zm) the form and manner of particulars about conversion under the proviso to paragraph 5 of the Fourth Schedule.
- (3) Every rule made under this Act by the Central Government 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.
80. (1) If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order published in the Official Gazette, make such provisions, not inconsistent with the provisions of this Act as may appear to it be necessary for removing the difficulty :
 Provided that no such order shall be made under this section after the expiry of a period of two years from the commencement of this Act.
- (2) Every order made under this section shall be laid, as soon as may be, after it is made, before each House of Parliament.
81. Until the Tribunal and the Appellate Tribunal are constituted under the provisions of the Companies Act, 1956, the provisions of this Act shall have effect subject to the following modifications, namely :-
- (a) for the word "Tribunal" occurring in clause (b) of sub-section (1) of section 41, clause (a) of sub-section (1) of section 43 and section 44, the words "Company Law Board" had been substituted;
 - (b) for the word "Tribunal" occurring in section 51 and in sections 60 to 64, the words "High Court" had been substituted;
 - (c) for the words "Appellate Tribunal" occurring in sub-section (2) of section 72, the words "High Court" had been substituted.



4.2 RIGHT TO INFORMATION ACT, 2005

An Act to provide for setting out the practical regime of right to information for citizens to secure access to information under the control of public authorities, in order to promote transparency and accountability in the working of every public authority, the constitution of a Central Information Commission and State Information Commissions and for matters connected therewith or incidental thereto.

1. INTRODUCTION

- (1) This Act may be called the Right to Information Act, 2005.
- (2) It extends to the whole of India except the State of Jammu and Kashmir.
- (3) The provisions of sub-section (1) of section 4, sub-sections (1) and (2) of section 5, sections 12, 13, 15, 16, 24, 27 and 28 shall come into force at once, and the remaining provisions of this Act shall come into force on the one hundred and twentieth day of its enactment.

2. DEFINITIONS

- (a) “appropriate Government” means in relation to a public authority which is established, constituted, owned, controlled or substantially financed by funds provided directly or indirectly—
 - (i) by the Central Government or the Union territory administration, the Central Government;
 - (ii) by the State Government, the State Government;
- (b) “Central Information Commission” means the Central Information Commission constituted under sub-section (1) of section 12;
- (c) “Central Public Information Officer” means the Central Public Information Officer designated under sub-section (1) and includes a Central Assistant Public Information Officer designated as such under sub-section (2) of section 5;
- (d) “Chief Information Commissioner” and “Information Commissioner” mean the Chief Information Commissioner and Information Commissioner appointed under sub-section (3) of section 12;
- (e) “competent authority” means—
 - (i) the Speaker in the case of the House of the People or the Legislative Assembly of a State or a Union territory having such Assembly and the Chairman in the case of the Council of States or Legislative Council of a State;
 - (ii) the Chief Justice of India in the case of the Supreme Court;
 - (iii) the Chief Justice of the High Court in the case of a High Court;
 - (iv) the President or the Governor, as the case may be, in the case of other authorities established or constituted by or under the Constitution;
 - (v) the administrator appointed under article 239 of the Constitution;
- (f) “information” means any material in any form, including records, documents, memos, e-mails, opinions, advices, press releases, circulars, orders, logbooks, contracts, reports, papers, samples, models, data material held in any electronic form and information relating to any private body which can be accessed by a public authority under any other law for the time being in force;
- (g) “prescribed” means prescribed by rules made under this Act by the appropriate Government or the competent authority, as the case may be;
- (h) “public authority” means any authority or body or institution of self- government established or constituted—
 - (a) by or under the Constitution;
 - (b) by any other law made by Parliament;
 - (c) by any other law made by State Legislature;
 - (d) by notification issued or order made by the appropriate Government, and includes any—
 - (i) body owned, controlled or substantially financed;



- (ii) non-Government organisation substantially financed, directly or indirectly by funds provided by the appropriate Government;
- (i) “record” includes—
 - (a) any document, manuscript and file;
 - (b) any microfilm, microfiche and facsimile copy of a document;
 - (c) any reproduction of image or images embodied in such microfilm (whether enlarged or not); and
 - (d) any other material produced by a computer or any other device;
- (j) “right to information” means the right to information accessible under this Act which is held by or under the control of any public authority and includes the right to—
 - (i) inspection of work, documents, records;
 - (ii) taking notes, extracts or certified copies of documents or records;
 - (iii) taking certified samples of material;
 - (iv) obtaining information in the form of diskettes, floppies, tapes, video cassettes or in any other electronic mode or through printouts where such information is stored in a computer or in any other device;
- (k) “State Information Commission” means the State Information Commission constituted under sub-section (1) of section 15;
- (l) “State Chief Information Commissioner” and “State Information Commissioner” mean the State Chief Information Commissioner and the State Information Commissioner appointed under sub-section (3) of section 15;
- (m) “State Public Information Officer” means the State Public Information Officer designated under sub-section (1) and includes a State Assistant Public Information Officer designated as such under sub-section (2) of section 5;
- (n) “third party” means a person other than the citizen making a request for information and includes a public authority.

RIGHT TO INFORMATION AND OBLIGATIONS OF PUBLIC AUTHORITIES

3. Subject to the provisions of this Act, all citizens shall have the right to information.

4. (1) Every public authority shall—

- (a) maintain all its records duly catalogued and indexed in a manner and the form which facilitates the right to information under this Act and ensure that all records that are appropriate to be computerised are, within a reasonable time and subject to availability of resources, computerised and connected through a network all over the country on different systems so that access to such records is facilitated;
- (b) publish within one hundred and twenty days from the enactment of this Act,—
 - (i) the particulars of its organisation, functions and duties;
 - (ii) the powers and duties of its officers and employees;
 - (iii) the procedure followed in the decision making process, including channels of supervision and accountability;
 - (iv) the norms set by it for the discharge of its functions;
 - (v) the rules, regulations, instructions, manuals and records, held by it or under its control or used by its employees for discharging its functions;
 - (vi) a statement of the categories of documents that are held by it or under its control;
 - (vii) the particulars of any arrangement that exists for consultation with, or representation by, the members of the public in relation to the formulation of its policy or implementation thereof;
 - (viii) a statement of the boards, councils, committees and other bodies consisting of two or more persons constituted as its part or for the purpose of its advice, and as to whether meetings of those boards, councils, committees and other bodies are open to the public, or the minutes of such meetings are accessible for public;



- (ix) a directory of its officers and employees;
 - (x) the monthly remuneration received by each of its officers and employees, including the system of compensation as provided in its regulations;
 - (xi) the budget allocated to each of its agency, indicating the particulars of all plans, proposed expenditures and reports on disbursements made;
 - (xii) the manner of execution of subsidy programmes, including the amounts allocated and the details of beneficiaries of such programmes;
 - (xiii) particulars of recipients of concessions, permits or authorisations granted by it;
 - (xiv) details in respect of the information, available to or held by it, reduced in an electronic form;
 - (xv) the particulars of facilities available to citizens for obtaining information, including the working hours of a library or reading room, if maintained for public use;
 - (xvi) the names, designations and other particulars of the Public Information Officers;
 - (xvii) such other information as may be prescribed; and thereafter update these publications every year;
 - (c) publish all relevant facts while formulating important policies or announcing the decisions which affect public;
 - (d) provide reasons for its administrative or quasi-judicial decisions to affected persons.
- (2) It shall be a constant endeavour of every public authority to take steps in accordance with the requirements of clause (b) of sub-section (1) to provide as much information suo motu to the public at regular intervals through various means of communications, including internet, so that the public have minimum resort to the use of this Act to obtain information.
- (3) For the purposes of sub-section (1), every information shall be disseminated widely and in such form and manner which is easily accessible to the public.
- (4) All materials shall be disseminated taking into consideration the cost effectiveness, local language and the most effective method of communication in that local area and the information should be easily accessible, to the extent possible in electronic format with the Central Public Information Officer or State Public Information Officer, as the case may be, available free or at such cost of the medium or the print cost price as may be prescribed.

Explanation : For the purposes of sub-sections (3) and (4), “disseminated” means making known or communicated the information to the public through notice boards, newspapers, public announcements, media broadcasts, the internet or any other means, including inspection of offices of any public authority.

5. (1) Every public authority shall, within one hundred days of the enactment of this Act, designate as many officers as the Central Public Information Officers or State Public Information Officers, as the case may be, in all administrative units or offices under it as may be necessary to provide information to persons requesting for the information under this Act.
- (2) Without prejudice to the provisions of sub-section (1), every public authority shall designate an officer, within one hundred days of the enactment of this Act, at each sub-divisional level or other sub-district level as a Central Assistant Public Information Officer or a State Assistant Public Information Officer, as the case may be, to receive the applications for information or appeals under this Act for forwarding the same forthwith to the Central Public Information Officer or the State Public Information Officer or senior officer specified under sub-section (1) of section 19 or the Central Information Commission or the State Information Commission, as the case may be:

Provided that where an application for information or appeal is given to a Central Assistant Public Information Officer or a State Assistant Public Information Officer, as the case may be, a period of five days shall be added in computing the period for response specified under sub-section (1) of section 7.

- (3) Every Central Public Information Officer or State Public Information Officer, as the case may be, shall deal with requests from persons seeking information and render reasonable assistance to the persons seeking such information.
- (4) The Central Public Information Officer or State Public Information Officer, as the case may be, may seek the assistance of any other officer as he or she considers it necessary for the proper discharge of his or her duties.



- (5) Any officer, whose assistance has been sought under sub-section (4), shall render all assistance to the Central Public Information Officer or State Public Information Officer, as the case may be, seeking his or her assistance and for the purposes of any contravention of the provisions of this Act, such other officer shall be treated as a Central Public Information Officer or State Public Information Officer, as the case may be.
6. (1) A person, who desires to obtain any information under this Act, shall make a request in writing or through electronic means in English or Hindi or in the official language of the area in which the application is being made, accompanying such fee as may be prescribed, to—

- (a) the Central Public Information Officer or State Public Information Officer, as the case may be, of the concerned public authority;
- (b) the Central Assistant Public Information Officer or State Assistant Public Information Officer, as the case may be, specifying the particulars of the information sought by him or her:

Provided that where such request cannot be made in writing, the Central Public Information Officer or State Public Information Officer, as the case may be, shall render all reasonable assistance to the person making the request orally to reduce the same in writing.

- (2) An applicant making request for information shall not be required to give any reason for requesting the information or any other personal details except those that may be necessary for contacting him.
- (3) Where an application is made to a public authority requesting for an information,—
 - (i) which is held by another public authority; or
 - (ii) the subject matter of which is more closely connected with the functions of another public authority, the public authority, to which such application is made, shall transfer the application or such part of it as may be appropriate to that other public authority and inform the applicant immediately about such transfer :

Provided that the transfer of an application pursuant to this sub-section shall be made as soon as practicable but in no case later than five days from the date of receipt of the application.

7. (1) Subject to the proviso to sub-section (2) of section 5 or the proviso to sub-section (3) of section 6, the Central Public Information Officer or State Public Information Officer, as the case may be, on receipt of a request under section 6 shall, as expeditiously as possible, and in any case within thirty days of the receipt of the request, either provide the information on payment of such fee as may be prescribed or reject the request for any of the reasons specified in sections 8 and 9:

Provided that where the information sought for concerns the life or liberty of a person, the same shall be provided within forty-eight hours of the receipt of the request.

- (2) If the Central Public Information Officer or State Public Information Officer, as the case may be, fails to give decision on the request for information within the period specified under sub-section (1), the Central Public Information Officer or State Public Information Officer, as the case may be, shall be deemed to have refused the request.
- (3) Where a decision is taken to provide the information on payment of any further fee representing the cost of providing the information, the Central Public Information Officer or State Public Information Officer, as the case may be, shall send an intimation to the person making the request, giving—
 - (a) the details of further fees representing the cost of providing the information as determined by him, together with the calculations made to arrive at the amount in accordance with fee prescribed under sub-section (1), requesting him to deposit that fees, and the period intervening between the dispatch of the said intimation and payment of fees shall be excluded for the purpose of calculating the period of thirty days referred to in that sub-section;
 - (b) information concerning his or her right with respect to review the decision as to the amount of fees charged or the form of access provided, including the particulars of the appellate authority, time limit, process and any other forms.
- (4) Where access to the record or a part thereof is required to be provided under this Act and the person to whom access is to be provided is sensorily disabled, the Central Public Information Officer or State Public Information Officer, as the case may be, shall provide assistance to enable access to the information, including providing such assistance as may be appropriate for the inspection.



- (5) Where access to information is to be provided in the printed or in any electronic format, the applicant shall, subject to the provisions of sub-section (6), pay such fee as may be prescribed:

Provided that the fee prescribed under sub-section (1) of section 6 and sub-sections (1) and (5) of section 7 shall be reasonable and no such fee shall be charged from the persons who are of below poverty line as may be determined by the appropriate Government.

- (6) Notwithstanding anything contained in sub-section (5), the person making request for the information shall be provided the information free of charge where a public authority fails to comply with the time limits specified in sub-section (1).
- (7) Before taking any decision under sub-section (1), the Central Public Information Officer or State Public Information Officer, as the case may be, shall take into consideration the representation made by a third party under section 11.
- (8) Where a request has been rejected under sub-section (1), the Central Public Information Officer or State Public Information Officer, as the case may be, shall communicate to the person making the request,—
- (i) the reasons for such rejection;
 - (ii) the period within which an appeal against such rejection may be preferred; and
 - (iii) the particulars of the appellate authority.
- (9) An information shall ordinarily be provided in the form in which it is sought unless it would disproportionately divert the resources of the public authority or would be detrimental to the safety or preservation of the record in question.

8. (1) Notwithstanding anything contained in this Act, there shall be no obligation to give any citizen,—

- (a) information, disclosure of which would prejudicially affect the sovereignty and integrity of India, the security, strategic, scientific or economic interests of the State, relation with foreign State or lead to incitement of an offence;
- (b) information which has been expressly forbidden to be published by any court of law or tribunal or the disclosure of which may constitute contempt of court;
- (c) information, the disclosure of which would cause a breach of privilege of Parliament or the State Legislature;
- (d) information including commercial confidence, trade secrets or intellectual property, the disclosure of which would harm the competitive position of a third party, unless the competent authority is satisfied that larger public interest warrants the disclosure of such information;
- (e) information available to a person in his fiduciary relationship, unless the competent authority is satisfied that the larger public interest warrants the disclosure of such information;
- (f) information received in confidence from foreign Government;
- (g) information, the disclosure of which would endanger the life or physical safety of any person or identify the source of information or assistance given in confidence for law enforcement or security purposes;
- (h) information which would impede the process of investigation or apprehension or prosecution of offenders;
- (i) cabinet papers including records of deliberations of the Council of Ministers, Secretaries and other officers;

Provided that the decisions of Council of Ministers, the reasons thereof, and the material on the basis of which the decisions were taken shall be made public after the decision has been taken, and the matter is complete, or over:

Provided further that those matters which come under the exemptions specified in this section shall not be disclosed;

- (j) information which relates to personal information the disclosure of which has no relationship to any public activity or interest, or which would cause unwarranted invasion of the privacy of the individual unless the Central Public Information Officer or the State Public Information Officer or the appellate authority, as the case may be, is satisfied that the larger public interest justifies the disclosure of such information:



Provided that the information which cannot be denied to the Parliament or a State Legislature shall not be denied to any person.

- (2) Notwithstanding anything in the Official Secrets Act, 1923 nor any of the exemptions permissible in accordance with sub-section (1), a public authority may allow access to information, if public interest in disclosure outweighs the harm to the protected interests.
- (3) Subject to the provisions of clauses (a), (c) and (i) of sub-section (1), any information relating to any occurrence, event or matter which has taken place, occurred or happened twenty years before the date on which any request is made under section 6 shall be provided to any person making a request under that section:

Provided that where any question arises as to the date from which the said period of twenty years has to be computed, the decision of the Central Government shall be final, subject to the usual appeals provided for in this Act.

9. Without prejudice to the provisions of section 8, a Central Public Information Officer or a State Public Information Officer, as the case may be, may reject a request for information where such a request for providing access would involve an infringement of copyright subsisting in a person other than the State.

SEVERABILITY

- 10.(1) Where a request for access to information is rejected on the ground that it is in relation to information which is exempt from disclosure, then, notwithstanding anything contained in this Act, access may be provided to that part of the record which does not contain any information which is exempt from disclosure under this Act and which can reasonably be severed from any part that contains exempt information.
- (2) Where access is granted to a part of the record under sub-section (1), the Central Public Information Officer or State Public Information Officer, as the case may be, shall give a notice to the applicant, informing—
 - (a) that only part of the record requested, after severance of the record containing information which is exempt from disclosure, is being provided;
 - (b) the reasons for the decision, including any findings on any material question of fact, referring to the material on which those findings were based;
 - (c) the name and designation of the person giving the decision;
 - (d) the details of the fees calculated by him or her and the amount of fee which the applicant is required to deposit; and
 - (e) his or her rights with respect to review of the decision regarding non-disclosure of part of the information, the amount of fee charged or the form of access provided, including the particulars of the senior officer specified under sub-section (1) of section 19 or the Central Information Commission or the State Information Commission, as the case may be, time limit, process and any other form of access.

THIRD PARTY INFORMATION

- 11.(1) Where a Central Public Information Officer or a State Public Information Officer, as the case may be, intends to disclose any information or record, or part thereof on a request made under this Act, which relates to or has been supplied by a third party and has been treated as confidential by that third party, the Central Public Information Officer or State Public Information Officer, as the case may be, shall, within five days from the receipt of the request, give a written notice to such third party of the request and of the fact that the Central Public Information Officer or State Public Information Officer, as the case may be, intends to disclose the information or record, or part thereof, and invite the third party to make a submission in writing or orally, regarding whether the information should be disclosed, and such submission of the third party shall be kept in view while taking a decision about disclosure of information: Provided that except in the case of trade or commercial secrets protected by law, disclosure may be allowed if the public interest in disclosure outweighs in importance any possible harm or injury to the interests of such third party.



- (2) Where a notice is served by the Central Public Information Officer or State Public Information Officer, as the case may be, under sub-section (1) to a third party in respect of any information or record or part thereof, the third party shall, within ten days from the date of receipt of such notice, be given the opportunity to make representation against the proposed disclosure.
- (3) Notwithstanding anything contained in section 7, the Central Public Information Officer or State Public Information Officer, as the case may be, shall, within forty days after receipt of the request under section 6, if the third party has been given an opportunity to make representation under sub-section (2), make a decision as to whether or not to disclose the information or record or part thereof and give in writing the notice of his decision to the third party.
- (4) A notice given under sub-section (3) shall include a statement that the third party to whom the notice is given is entitled to prefer an appeal under section 19 against the decision.

THE CENTRAL INFORMATION COMMISSION

12. (1) The Central Government shall, by notification in the Official Gazette, constitute a body to be known as the Central Information Commission to exercise the powers conferred on, and to perform the functions assigned to, it under this Act.
 - (2) The Central Information Commission shall consist of—
 - (a) the Chief Information Commissioner; and
 - (b) such number of Central Information Commissioners, not exceeding ten, as may be deemed necessary.
 - (3) The Chief Information Commissioner and Information Commissioners shall be appointed by the President on the recommendation of a committee consisting of—
 - (i) the Prime Minister, who shall be the Chairperson of the committee;
 - (ii) the Leader of Opposition in the Lok Sabha; and
 - (iii) a Union Cabinet Minister to be nominated by the Prime Minister.
- Explanation :** For the purposes of removal of doubts, it is hereby declared that where the Leader of Opposition in the House of the People has not been recognised as such, the Leader of the single largest group in opposition of the Government in the House of the People shall be deemed to be the Leader of Opposition.
- (4) The general superintendence, direction and management of the affairs of the Central Information Commission shall vest in the Chief Information Commissioner who shall be assisted by the Information Commissioners and may exercise all such powers and do all such acts and things which may be exercised or done by the Central Information Commission autonomously without being subjected to directions by any other authority under this Act.
 - (5) The Chief Information Commissioner and Information Commissioners shall be persons of eminence in public life with wide knowledge and experience in law, science and technology, social service, management, journalism, mass media or administration and governance.
 - (6) The Chief Information Commissioner or an Information Commissioner shall not be a Member of Parliament or Member of the Legislature of any State or Union territory, as the case may be, or hold any other office of profit or connected with any political party or carrying on any business or pursuing any profession.
 - (7) The headquarters of the Central Information Commission shall be at Delhi and the Central Information Commission may, with the previous approval of the Central Government, establish offices at other places in India.
13. (1) The Chief Information Commissioner shall hold office for a term of five years from the date on which he enters upon his office and shall not be eligible for reappointment:
Provided that no Chief Information Commissioner shall hold office as such after he has attained the age of sixty-five years.
 - (2) Every Information Commissioner shall hold office for a term of five years from the date on which he enters upon his office or till he attains the age of sixty-five years, whichever is earlier, and shall not be eligible for reappointment as such Information Commissioner:



Provided that every Information Commissioner shall, on vacating his office under this sub-section be eligible for appointment as the Chief Information Commissioner in the manner specified in sub-section (3) of section 12:

Provided further that where the Information Commissioner is appointed as the Chief Information Commissioner, his term of office shall not be more than five years in aggregate as the Information Commissioner and the Chief Information Commissioner.

- (3) The Chief Information Commissioner or an Information Commissioner shall before he enters upon his office make and subscribe before the President or some other person appointed by him in that behalf, an oath or affirmation according to the form set out for the purpose in the First Schedule.
- (4) The Chief Information Commissioner or an Information Commissioner may, at any time, by writing under his hand addressed to the President, resign from his office:

Provided that the Chief Information Commissioner or an Information Commissioner may be removed in the manner specified under section 14.

- (5) The salaries and allowances payable to and other terms and conditions of service of—
 - (a) the Chief Information Commissioner shall be the same as that of the Chief Election Commissioner;
 - (b) an Information Commissioner shall be the same as that of an Election Commissioner:

Provided that if the Chief Information Commissioner or an Information Commissioner, at the time of his appointment is, in receipt of a pension, other than a disability or wound pension, in respect of any previous service under the Government of India or under the Government of a State, his salary in respect of the service as the Chief Information Commissioner or an Information Commissioner shall be reduced by the amount of that pension including any portion of pension which was commuted and pension equivalent of other forms of retirement benefits excluding pension equivalent of retirement gratuity:

Provided further that if the Chief Information Commissioner or an Information Commissioner if, at the time of his appointment is, in receipt of retirement benefits in respect of any previous service rendered in a Corporation established by or under any Central Act or State Act or a Government company owned or controlled by the Central Government or the State Government, his salary in respect of the service as the Chief Information Commissioner or an Information Commissioner shall be reduced by the amount of pension equivalent to the retirement benefits:

Provided also that the salaries, allowances and other conditions of service of the Chief Information Commissioner and the Information Commissioners shall not be varied to their disadvantage after their appointment.

- (6) The Central Government shall provide the Chief Information Commissioner and the Information Commissioners with such officers and employees as may be necessary for the efficient performance of their functions under this Act, and the salaries and allowances payable to and the terms and conditions of service of the officers and other employees appointed for the purpose of this Act shall be such as may be prescribed.
- 14.(1)** Subject to the provisions of sub-section (3), the Chief Information Commissioner or any Information Commissioner shall be removed from his office only by order of the President on the ground of proved misbehaviour or incapacity after the Supreme Court, on a reference made to it by the President, has, on inquiry, reported that the Chief Information Commissioner or any Information Commissioner, as the case may be, ought on such ground be removed.
- (2) The President may suspend from office, and if deem necessary prohibit also from attending the office during inquiry, the Chief Information Commissioner or Information Commissioner in respect of whom a reference has been made to the Supreme Court under sub-section (1) until the President has passed orders on receipt of the report of the Supreme Court on such reference.
 - (3) Notwithstanding anything contained in sub-section (1), the President may by order remove from office the Chief Information Commissioner or any Information Commissioner if the Chief Information Commissioner or a Information Commissioner, as the case may be,—
 - (a) is adjudged an insolvent; or



- (b) has been convicted of an offence which, in the opinion of the President, involves moral turpitude; or
 - (c) engages during his term of office in any paid employment outside the duties of his office; or
 - (d) is, in the opinion of the President, unfit to continue in office by reason of infirmity of mind or body; or
 - (e) has acquired such financial or other interest as is likely to affect prejudicially his functions as the Chief Information Commissioner or a Information Commissioner.
- (4) If the Chief Information Commissioner or a Information Commissioner in any way, concerned or interested in any contract or agreement made by or on behalf of the Government of India or participates in any way in the profit thereof or in any benefit or emolument arising therefrom otherwise than as a member and in common with the other members of an incorporated company, he shall, for the purposes of sub-section (1), be deemed to be guilty of misbehaviour.

THE STATE INFORMATION COMMISSION

CONSTITUTION OF STATE INFORMATION COMMISSION

15. (1) Every State Government shall, by notification in the Official Gazette, constitute a body to be known as the (name of the State) Information Commission to exercise the powers conferred on, and to perform the functions assigned to, it under this Act.
- (2) The State Information Commission shall consist of—
- (a) the State Chief Information Commissioner, and
 - (b) such number of State Information Commissioners, not exceeding ten, as may be deemed necessary.
- (3) The State Chief Information Commissioner and the State Information Commissioners shall be appointed by the Governor on the recommendation of a committee consisting of—
- (i) the Chief Minister, who shall be the Chairperson of the committee;
 - (ii) the Leader of Opposition in the Legislative Assembly; and
 - (iii) a Cabinet Minister to be nominated by the Chief Minister

Explanation.—For the purposes of removal of doubts, it is hereby declared that where the Leader of Opposition in the Legislative Assembly has not been recognised as such, the Leader of the single largest group in opposition of the Government in the Legislative Assembly shall be deemed to be the Leader of Opposition.

- (4) The general superintendence, direction and management of the affairs of the State Information Commission shall vest in the State Chief Information Commissioner who shall be assisted by the State Information Commissioners and may exercise all such powers and do all such acts and things which may be exercised or done by the State Information Commission autonomously without being subjected to directions by any other authority under this Act.
- (5) The State Chief Information Commissioner and the State Information Commissioners shall be persons of eminence in public life with wide knowledge and experience in law, science and technology, social service, management, journalism, mass media or administration and governance.
- (6) The State Chief Information Commissioner or a State Information Commissioner shall not be a Member of Parliament or Member of the Legislature of any State or Union territory, as the case may be, or hold any other office of profit or connected with any political party or carrying on any business or pursuing any profession.
- (7) The headquarters of the State Information Commission shall be at such place in the State as the State Government may, by notification in the Official Gazette, specify and the State Information Commission may, with the previous approval of the State Government, establish offices at other places in the State.

TERM OF OFFICE AND CONDITIONS OF SERVICE

16. (1) The State Chief Information Commissioner shall hold office for a term of five years from the date on which he enters upon his office and shall not be eligible for reappointment:



Provided that no State Chief Information Commissioner shall hold office as such after he has attained the age of sixty-five years.

- (2) Every State Information Commissioner shall hold office for a term of five years from the date on which he enters upon his office or till he attains the age of sixty-five years, whichever is earlier, and shall not be eligible for reappointment as such State Information Commissioner:

Provided that every State Information Commissioner shall, on vacating his office under this sub-section, be eligible for appointment as the State Chief Information Commissioner in the manner specified in sub-section (3) of section 15:

Provided further that where the State Information Commissioner is appointed as the State Chief Information Commissioner, his term of office shall not be more than five years in aggregate as the State Information Commissioner and the State Chief Information Commissioner.

- (3) The State Chief Information Commissioner or a State Information Commissioner, shall before he enters upon his office make and subscribe before the Governor or some other person appointed by him in that behalf, an oath or affirmation according to the form set out for the purpose in the First Schedule.
- (4) The State Chief Information Commissioner or a State Information Commissioner may, at any time, by writing under his hand addressed to the Governor, resign from his office:

Provided that the State Chief Information Commissioner or a State Information Commissioner may be removed in the manner specified under section 17.

- (5) The salaries and allowances payable to and other terms and conditions of service of—
- the State Chief Information Commissioner shall be the same as that of an Election Commissioner;
 - the State Information Commissioner shall be the same as that of the Chief Secretary to the State Government:

Provided that if the State Chief Information Commissioner or a State Information Commissioner, at the time of his appointment is, in receipt of a pension, other than a disability or wound pension, in respect of any previous service under the Government of India or under the Government of a State, his salary in respect of the service as the State Chief Information Commissioner or a State Information Commissioner shall be reduced by the amount of that pension including any portion of pension which was commuted and pension equivalent of other forms of retirement benefits excluding pension equivalent of retirement gratuity:

Provided further that where the State Chief Information Commissioner or a State Information Commissioner if, at the time of his appointment is, in receipt of retirement benefits in respect of any previous service rendered in a Corporation established by or under any Central Act or State Act or a Government company owned or controlled by the Central Government or the State Government, his salary in respect of the service as the State Chief Information Commissioner or the State Information Commissioner shall be reduced by the amount of pension equivalent to the retirement benefits:

Provided also that the salaries, allowances and other conditions of service of the State Chief Information Commissioner and the State Information Commissioners shall not be varied to their disadvantage after their appointment.

- (6) The State Government shall provide the State Chief Information Commissioner and the State Information Commissioners with such officers and employees as may be necessary for the efficient performance of their functions under this Act, and the salaries and allowances payable to and the terms and conditions of service of the officers and other employees appointed for the purpose of this Act shall be such as may be prescribed.

- 17.(1) Subject to the provisions of sub-section (3), the State Chief Information Commissioner or a State Information Commissioner shall be removed from his office only by order of the Governor on the ground of proved misbehaviour or incapacity after the Supreme Court, on a reference made to it by the Governor, has on inquiry, reported that the State Chief Information Commissioner or a State Information Commissioner, as the case may be, ought on such ground be removed.
- (2) The Governor may suspend from office, and if deem necessary prohibit also from attending the office during inquiry, the State Chief Information Commissioner or a State Information Commissioner in respect of whom a reference has been made to the Supreme Court under sub-section (1) until the Governor has passed orders on receipt of the report of the Supreme Court on such reference.



- (3) Notwithstanding anything contained in sub-section (1), the Governor may by order remove from office the State Chief Information Commissioner or a State Information Commissioner if a State Chief Information Commissioner or a State Information Commissioner, as the case may be,—
- (a) is adjudged an insolvent; or
 - (b) has been convicted of an offence which, in the opinion of the Governor, involves moral turpitude; or
 - (c) engages during his term of office in any paid employment outside the duties of his office; or
 - (d) is, in the opinion of the Governor, unfit to continue in office by reason of infirmity of mind or body; or
 - (e) has acquired such financial or other interest as is likely to affect prejudicially his functions as the State Chief Information Commissioner or a State Information Commissioner.
- (4) If the State Chief Information Commissioner or a State Information Commissioner in any way, concerned or interested in any contract or agreement made by or on behalf of the Government of the State or participates in any way in the profit thereof or in any benefit or emoluments arising therefrom otherwise than as a member and in common with the other members of an incorporated company, he shall, for the purposes of sub-section (1), be deemed to be guilty of misbehaviour.

POWERS AND FUNCTIONS OF THE INFORMATION COMMISSIONS, APPEAL AND PENALTIES

- 18.** (1) Subject to the provisions of this Act, it shall be the duty of the Central Information Commission or State Information Commission, as the case may be, to receive and inquire into a complaint from any person,—
- (a) who has been unable to submit a request to a Central Public Information Officer or State Public Information Officer, as the case may be, either by reason that no such officer has been appointed under this Act, or because the Central Assistant Public Information Officer or State Assistant Public Information Officer, as the case may be, has refused to accept his or her application for information or appeal under this Act for forwarding the same to the Central Public Information Officer or State Public Information Officer or senior officer specified in sub-section (1) of section 19 or the Central Information Commission or the State Information Commission, as the case may be;
 - (b) who has been refused access to any information requested under this Act;
 - (c) who has not been given a response to a request for information or access to information within the time limit specified under this Act;
 - (d) who has been required to pay an amount of fee which he or she considers unreasonable;
 - (e) who believes that he or she has been given incomplete, misleading or false information under this Act; and
 - (f) in respect of any other matter relating to requesting or obtaining access to records under this Act.
- (2) Where the Central Information Commission or State Information Commission, as the case may be, is satisfied that there are reasonable grounds to inquire into the matter, it may initiate an inquiry in respect thereof.
- (3) The Central Information Commission or State Information Commission, as the case may be, shall, while inquiring into any matter under this section, have the same powers as are vested in a civil court while trying a suit under the Code of Civil Procedure, 1908, in respect of the following matters, namely:—
- (a) summoning and enforcing the attendance of persons and compel them to give oral or written evidence on oath and to produce the documents or things;
 - (b) requiring the discovery and inspection of documents;
 - (c) receiving evidence on affidavit;
 - (d) requisitioning any public record or copies thereof from any court or office;
 - (e) issuing summons for examination of witnesses or documents; and
 - (f) any other matter which may be prescribed.
- (4) Notwithstanding anything inconsistent contained in any other Act of Parliament or State Legislature, as the case may be, the Central Information Commission or the State Information Commission, as the case may be, may, during the inquiry of any complaint under this Act, examine any record to which this



Act applies which is under the control of the public authority, and no such record may be withheld from it on any grounds.

APPEAL

- 19.** (1) Any person who, does not receive a decision within the time specified in sub-section (1) or clause (a) of sub-section (3) of section 7, or is aggrieved by a decision of the Central Public Information Officer or State Public Information Officer, as the case may be, may within thirty days from the expiry of such period or from the receipt of such a decision prefer an appeal to such officer who is senior in rank to the Central Public Information Officer or State Public Information Officer as the case may be, in each public authority:

Provided that such officer may admit the appeal after the expiry of the period of thirty days if he or she is satisfied that the appellant was prevented by sufficient cause from filing the appeal in time.

- (2) Where an appeal is preferred against an order made by a Central Public Information Officer or a State Public Information Officer, as the case may be, under section 11 to disclose third party information, the appeal by the concerned third party shall be made within thirty days from the date of the order.
- (3) A second appeal against the decision under sub-section (1) shall lie within ninety days from the date on which the decision should have been made or was actually received, with the Central Information Commission or the State Information Commission:

Provided that the Central Information Commission or the State Information Commission, as the case may be, may admit the appeal after the expiry of the period of ninety days if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal in time.

- (4) If the decision of the Central Public Information Officer or State Public Information Officer, as the case may be, against which an appeal is preferred relates to information of a third party, the Central Information Commission or State Information Commission, as the case may be, shall give a reasonable opportunity of being heard to that third party.
- (5) In any appeal proceedings, the onus to prove that a denial of a request was justified shall be on the Central Public Information Officer or State Public Information Officer, as the case may be, who denied the request.
- (6) An appeal under sub-section (1) or sub-section (2) shall be disposed of within thirty days of the receipt of the appeal or within such extended period not exceeding a total of forty-five days from the date of filing thereof, as the case may be, for reasons to be recorded in writing.
- (7) The decision of the Central Information Commission or State Information Commission, as the case may be, shall be binding.
- (8) In its decision, the Central Information Commission or State Information Commission, as the case may be, has the power to—
- (a) require the public authority to take any such steps as may be necessary to secure compliance with the provisions of this Act, including—
 - (i) by providing access to information, if so requested, in a particular form;
 - (ii) by appointing a Central Public Information Officer or State Public Information Officer, as the case may be;
 - (iii) by publishing certain information or categories of information;
 - (iv) by making necessary changes to its practices in relation to the maintenance, management and destruction of records;
 - (v) by enhancing the provision of training on the right to information for its officials;
 - (vi) by providing it with an annual report in compliance with clause (b) of sub-section (1) of section 4;
 - (b) require the public authority to compensate the complainant for any loss or other detriment suffered;
 - (c) impose any of the penalties provided under this Act;
 - (d) reject the application.



- (9) The Central Information Commission or State Information Commission, as the case may be, shall give notice of its decision, including any right of appeal, to the complainant and the public authority.
- (10) The Central Information Commission or State Information Commission, as the case may be, shall decide the appeal in accordance with such procedure as may be prescribed.

PENALTIES

- 20.** (1) Where the Central Information Commission or the State Information Commission, as the case may be, at the time of deciding any complaint or appeal is of the opinion that the Central Public Information Officer or the State Public Information Officer, as the case may be, has, without any reasonable cause, refused to receive an application for information or has not furnished information within the time specified under sub-section (1) of section 7 or malafidely denied the request for information or knowingly given incorrect, incomplete or misleading information or destroyed information which was the subject of the request or obstructed in any manner in furnishing the information, it shall impose a penalty of two hundred and fifty rupees each day till application is received or information is furnished, so however, the total amount of such penalty shall not exceed twenty-five thousand rupees:

Provided that the Central Public Information Officer or the State Public Information Officer, as the case may be, shall be given a reasonable opportunity of being heard before any penalty is imposed on him:

Provided further that the burden of proving that he acted reasonably and diligently shall be on the Central Public Information Officer or the State Public Information Officer, as the case may be.

- (2) Where the Central Information Commission or the State Information Commission, as the case may be, at the time of deciding any complaint or appeal is of the opinion that the Central Public Information Officer or the State Public Information Officer, as the case may be, has, without any reasonable cause and persistently, failed to receive an application for information or has not furnished information within the time specified under sub-section (1) of section 7 or malafidely denied the request for information or knowingly given incorrect, incomplete or misleading information or destroyed information which was the subject of the request or obstructed in any manner in furnishing the information, it shall recommend for disciplinary action against the Central Public Information Officer or the State Public Information Officer, as the case may be, under the service rules applicable to him.

PROTECTION OF ACTION TAKEN IN GOOD FAITH.

- 21.** No suit, prosecution or other legal proceeding shall lie against any person for anything which is in good faith done or intended to be done under this Act or any rule made thereunder.

ACT TO HAVE OVERRIDING EFFECT

- 22.** The provisions of this Act shall have effect notwithstanding anything inconsistent therewith contained in the Official Secrets Act, 1923, and any other law for the time being in force or in any instrument having effect by virtue of any law other than this Act.

BAR OF JURISDICTION OF COURTS

- 23.** No court shall entertain any suit, application or other proceeding in respect of any order made under this Act and no such order shall be called in question otherwise than by way of an appeal under this Act.

ACT NOT TO APPLY TO CERTAIN ORGANIZATIONS

- 24.** (1) Nothing contained in this Act shall apply to the intelligence and security organisations specified in the Second Schedule, being organisations established by the Central Government or any information furnished by such organisations to that Government:

Provided that the information pertaining to the allegations of corruption and human rights violations shall not be excluded under this sub-section:

Provided further that in the case of information sought for is in respect of allegations of violation of human rights, the information shall only be provided after the approval of the Central Information



Commission, and notwithstanding anything contained in section 7, such information shall be provided within forty-five days from the date of the receipt of request.

- (2) The Central Government may, by notification in the Official Gazette, amend the Schedule by including therein any other intelligence or security organisation established by that Government or omitting therefrom any organisation already specified therein and on the publication of such notification, such organisation shall be deemed to be included in or, as the case may be, omitted from the Schedule.
- (3) Every notification issued under sub-section (2) shall be laid before each House of Parliament.
- (4) Nothing contained in this Act shall apply to such intelligence and security organisation being organisations established by the State Government, as that Government may, from time to time, by notification in the Official Gazette, specify:

Provided that the information pertaining to the allegations of corruption and human rights violations shall not be excluded under this sub-section:

Provided further that in the case of information sought for is in respect of allegations of violation of human rights, the information shall only be provided after the approval of the State Information Commission and, notwithstanding anything contained in section 7, such information shall be provided within forty-five days from the date of the receipt of request.

- (5) Every notification issued under sub-section (4) shall be laid before the State Legislature.
- 25.** (1) The Central Information Commission or State Information Commission, as the case may be, shall, as soon as practicable after the end of each year, prepare a report on the implementation of the provisions of this Act during that year and forward a copy thereof to the appropriate Government.
- (2) Each Ministry or Department shall, in relation to the public authorities within their jurisdiction, collect and provide such information to the Central Information Commission or State Information Commission, as the case may be, as is required to prepare the report under this section and comply with the requirements concerning the furnishing of that information and keeping of records for the purposes of this section.
 - (3) Each report shall state in respect of the year to which the report relates,—
 - (a) the number of requests made to each public authority;
 - (b) the number of decisions where applicants were not entitled to access to the documents pursuant to the requests, the provisions of this Act under which these decisions were made and the number of times such provisions were invoked;
 - (c) the number of appeals referred to the Central Information Commission or State Information Commission, as the case may be, for review, the nature of the appeals and the outcome of the appeals;
 - (d) particulars of any disciplinary action taken against any officer in respect of the administration of this Act;
 - (e) the amount of charges collected by each public authority under this Act;
 - (f) any facts which indicate an effort by the public authorities to administer and implement the spirit and intention of this Act;
 - (g) recommendations for reform, including recommendations in respect of the particular public authorities, for the development, improvement, modernisation, reform or amendment to this Act or other legislation or common law or any other matter relevant for operationalising the right to access information.
 - (4) The Central Government or the State Government, as the case may be, may, as soon as practicable after the end of each year, cause a copy of the report of the Central Information Commission or the State Information Commission, as the case may be, referred to in sub-section (1) to be laid before each House of Parliament or, as the case may be, before each House of the State Legislature, where there are two Houses, and where there is one House of the State Legislature before that House.
 - (5) If it appears to the Central Information Commission or State Information Commission, as the case may be, that the practice of a public authority in relation to the exercise of its functions under this Act does not conform with the provisions or spirit of this Act, it may give to the authority a recommendation specifying the steps which ought in its opinion to be taken for promoting such conformity.



APPROPRIATE GOVERNMENT TO PREPARE PROGRAMMES

- 26.** (1) The appropriate Government may, to the extent of availability of financial and other resources,—
- (a) develop and organise educational programmes to advance the understanding of the public, in particular of disadvantaged communities as to how to exercise the rights contemplated under this Act;
 - (b) encourage public authorities to participate in the development and organisation of programmes referred to in clause (a) and to undertake such programmes themselves;
 - (c) promote timely and effective dissemination of accurate information by public authorities about their activities; and
 - (d) train Central Public Information Officers or State Public Information Officers, as the case may be, of public authorities and produce relevant training materials for use by the public authorities themselves.
- (2) The appropriate Government shall, within eighteen months from the commencement of this Act, compile in its official language a guide containing such information, in an easily comprehensible form and manner, as may reasonably be required by a person who wishes to exercise any right specified in this Act.
- (3) The appropriate Government shall, if necessary, update and publish the guidelines referred to in sub-section (2) at regular intervals which shall, in particular and without prejudice to the generality of sub-section (2), include—
- (a) the objects of this Act;
 - (b) the postal and street address, the phone and fax number and, if available, electronic mail address of the Central Public Information Officer or State Public Information Officer, as the case may be, of every public authority appointed under sub-section (1) of section 5;
 - (c) the manner and the form in which request for access to an information shall be made to a Central Public Information Officer or State Public Information Officer, as the case may be;
 - (d) the assistance available from and the duties of the Central Public Information Officer or State Public Information Officer, as the case may be, of a public authority under this Act;
 - (e) the assistance available from the Central Information Commission or State Information Commission, as the case may be;
 - (f) all remedies in law available regarding an act or failure to act in respect of a right or duty conferred or imposed by this Act including the manner of filing an appeal to the Commission;
 - (g) the provisions providing for the voluntary disclosure of categories of records in accordance with section 4;
 - (h) the notices regarding fees to be paid in relation to requests for access to an information; and
 - (i) any additional regulations or circulars made or issued in relation to obtaining access to an information in accordance with this Act.
- (4) The appropriate Government must, if necessary, update and publish the guidelines at regular intervals.
- 27.** (1) The appropriate Government may, by notification in the Official Gazette, make rules to carry out the provisions of this Act.
- (2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely :—
- (a) the cost of the medium or print cost price of the materials to be disseminated under sub-section (4) of section 4;
 - (b) the fee payable under sub-section (1) of section 6;
 - (c) the fee payable under sub-sections (1) and (5) of section 7;
 - (d) the salaries and allowances payable to and the terms and conditions of service of the officers and other employees under sub-section (6) of section 13 and sub-section (6) of section 16;
 - (e) the procedure to be adopted by the Central Information Commission or State Information



Commission, as the case may be, in deciding the appeals under Information Commission, as the case may be, in deciding the appeals under sub-section (10) of section 19; and

(f) any other matter which is required to be, or may be, prescribed.

- 28.** (1) The competent authority may, by notification in the Official Gazette, make rules to carry out the provisions of this Act.
- (2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely :-
- (i) the cost of the medium of print cost price of the material to be disseminated under sub-section (4) of section 4;
 - (ii) the fee payable under sub-section (1) of section 6;
 - (iii) the fee payable under sub-section (1) of section 7; and
 - (iv) any other matter which is required to be, or may be, prescribed
- 29.** (1) 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.
- (2) Every rule made under this Act by a State Government shall be laid, as soon as may be after it is notified, before the State Legislature.
- 30.** (1) If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order published in the Official Gazette, make such provisions not inconsistent with the provisions of this Act as appear to it to be necessary or expenditure for removal of the difficulty :
- Provided that no such order shall be made after the expiry of a period of two years from the date of the commencement of this Act.
- (2) Every order made under this section shall, as soon as may be after it is made, be laid before each House of Parliament.



4.3 THE COMPETITION ACT, 2002

The Competition Commission of India was established in October 2003 under the Competition Act, 2002. It was, however, mired in litigation as the provisions governing its functions were challenged in a writ petition before the Supreme Court.

The apex court in January 2005 addressed the writ petition with certain directions to the government. Consequent to this, the Competition (Amendment) Bill, 2006 was introduced in March 2006, and was referred for examination to the parliamentary standing committee.

Following the recommendations of the committee, the Competition (Amendment) Bill, 2007 was introduced and passed in August 2007. Further amendment was made in 2009 under Competition (Amendment) Act, 2009.

The backdrop

To achieve its objective of not permitting an 'appreciable adverse effect on competition in India', the Competition Act, 2002 deals with three situations—prohibition of anti-competitive agreements and abuse of dominant position, and regulation of combinations (covered acquisitions, mergers and amalgamations).

The focus of this article is the recent amendments dealing with two aspects of the third situation, which merit special attention—a change in threshold limits to meet the criteria for intimating the Competition Commission, and making such reporting mandatory.

Domestic nexus

An acquisition or merger or amalgamation would be governed under the third situation, if it constitutes a 'combination' by exceeding certain prescribed threshold limits. The limits determine the trigger for reporting the proposed combination to the commission.

The amendment focuses on the provision of a domestic nexus (a nexus with assets and operations in India) in connection with the limits applicable to acquisitions in which a foreign entity and an Indian entity are involved. This would narrow down the scope for an acquisition being covered under 'combinations' to be regulated by the commission. Thus, if the acquirer is a foreign company without any Indian presence, the Competition Act trigger will not apply due to the provision of the India nexus.

Incidentally, the original limits continue to apply under the Competition Act to acquisitions of enterprises dealing in similar goods, and to mergers and amalgamations.

A corresponding amendment in the limits has not been made for those cases. The rationale for this is not very clear because it would have been better to restrict the applicability to all cases of combinations.

Intimation mandatory

A very crucial aspect of the original provisions was that it was voluntary for an enterprise proposing to enter into a combination to intimate the Competition Commission. Now, once the new law comes into force, such intimation of the combination to the commission would be mandatory and, in fact, such a coupling shall not take effect until 210 days from the date of notification or approval from the commission, whichever is earlier.

This is likely to result in a long gestation period of about seven to eight months from the date of approval of the proposal. This has some critical dimensions to be considered. Any uncertainty in a merger/acquisition could have a serious and destabilizing impact on the businesses of the parties involved. In most cases, unlike an acquisition, a merger is dependent on the high court's approval (or, in the case of certain specified industries, any other regulatory body, such as the Reserve Bank of India in the case of banks).

The introduction of this new dimension of keeping the merger/acquisition pending until the approval of the commission will also (albeit for a different purpose) add a significant element of uncertainty, and can be a serious drag on 'big-ticket' M&A activities in India. The uncertainty has several implications, including the following:

- Perception among customers
- Uncertainty as regards the 'identity' of the enterprise could create reluctance among customers, who could choose to shift to a more 'stable' competitor.



- Inability to make strategic and operational decisions: Strategic and operational business issues could remain in 'limbo'.
- Human resources: In any acquisition or merger, the human resources element is crucial. This has dimensions relating to alignment of titles, roles and responsibilities. A long period of uncertainty could seriously dent morale and heighten attrition.
- Enterprise value(s): As a result of the uncertainty, including the above factors, the market value of both enterprises could be severely dented due to the long period of uncertainty. Interestingly, while such reference to a regulatory body is mandatory in a number of countries, the time limit prescribed by most of them is much shorter, ranging from 25-35 days for an initial investigation. When the initial investigation results in serious doubts regarding its effect on competition, the next level investigation triggers the time limit, which is generally 90-180 days. For example, in the US and the European Union, the time limit for initial investigation is 30 days and 25 days, and for detailed investigation, an additional 30 days and 90 days, respectively.

Summing up

While the objective of the Competition Act, 2002, as stated in its preamble, is undoubtedly laudable, the timing issue needs to be addressed. In addition, it is very important to have detailed guidelines and a framework within which the approval would be given by the Competition Commission. This could help mitigate the likely element of uncertainty by an upfront evaluation of the parameters contained in the guidelines in connection with the planned combination. One hopes the government will take such issues seriously and take steps to address them.

THE COMPETITION ACT, 2002

No. 12 OF 2003

An Act 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 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.

EXTENT

- (1) This Act may be called the Competition Act, 2002.
- (2) It extends to the whole of India except the State of Jammu and Kashmir.
- (3) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint:

Provided that different dates may be appointed for different provisions of this Act and any reference in any such provision to the commencement of this Act shall be construed as a reference to the coming into force of that provision.

DEFINITIONS

- (a) "acquisition" means, directly or indirectly, acquiring or agreeing to acquire—
 - (i) shares, voting rights or assets of any enterprise; or
 - (ii) control over management or control over assets of any enterprise;
- (b) "agreement" includes any arrangement or understanding or action in concert,—
 - (i) whether or not, such arrangement, understanding or action is formal or in writing; or
 - (ii) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings;
- (c) "cartel" includes an association of producers, sellers, 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;
- (d) "Chairperson" means the Chairperson of the Commission appointed under sub-section (1) of section 8;
- (e) "Commission" means the Competition Commission of India established under subsection (1) of section 7;
- (f) "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 partly paid or partly 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 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 whether such hiring or availing of services is for any commercial purpose or for personal use;
- (g) “Director General” means the Director General appointed under sub-section (1) of section 16 and includes any Additional, Joint, Deputy or Assistant Directors General appointed under that section;
- (h) “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.

Explanation—For the purposes of this clause,—

- (a) “activity” includes profession or occupation;
- (b) “article” includes a new article and “service” includes a new service;
- (c) “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;
- (i) “goods” means goods as defined in the Sale of Goods Act, 1930 and includes—
 - (A) products manufactured, processed or mined;
 - (B) debentures, stocks and shares after allotment;
 - (C) in relation to goods supplied, distributed or controlled in India, goods imported into India;
- (j) “Member” means a Member of the Commission appointed under sub-section (1) of section 8 and includes the Chairperson;
- (k) “notification” means a notification published in the Official Gazette;
- (l) “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, in India or outside India;
 - (vi) 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;
 - (vii) any body corporate incorporated by or under the laws of a country outside India;



- (viii) a co-operative society registered under any law relating to cooperative societies;
- (ix) a local authority;
- (x) every artificial juridical person, not falling within any of the preceding sub-clauses;
- (m) “practice” includes any practice relating to the carrying on of any trade by a person or an enterprise;
- (n) “prescribed” means prescribed by rules made under this Act;
- (o) “price”, in relation to the sale of any goods or to the performance of any services, includes every valuable consideration, whether direct or indirect, or deferred, and includes any consideration which in effect relates to the sale of any goods or to the performance of any services although ostensibly relating to any other matter or thing;
- (p) “public financial institution” means a public financial institution specified under section 4A of the Companies Act, 1956 and includes a State Financial, Industrial or Investment Corporation;
- (q) “regulations” means the regulations made by the Commission under section 64;
- (r) “relevant market” means the market which may be determined by the Commission with reference to the relevant product market or the relevant geographic market or with reference to both the markets;
- (s) “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 the conditions prevailing in the neighbouring areas;
- (t) “relevant product market” means a market comprising all those products or services which are regarded as interchangeable or substitutable by the consumer, by reason of characteristics of the products or services, their prices and intended use;
- (u) “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;
- (v) “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;
- (w) “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;
- (x) “trade” means any trade, business, industry, profession or occupation relating to the production, supply, distribution, storage or control of goods and includes the provision of any services;
- (y) “turnover” includes value of sale of goods or services;
- (z) words and expressions used but not defined in this Act and defined in the Companies Act, 1956 shall have the same meanings respectively assigned to them in that Act.

PROHIBITION OF CERTAIN AGREEMENTS, ABUSE OF DOMINANT POSITION AND REGULATION OF COMBINATIONS

Prohibition of agreements

Anti competitive agreements (Sec. 3)

- (1) 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 within India.

- (2) Any agreement entered into in contravention of the provisions contained in subsection (1) shall be void.
- (3) Any agreement entered into between enterprises or associations of enterprises or persons or associations of persons or between any person and enterprise or practice carried on, or decision taken by, any association of enterprises or association of persons, including cartels, engaged in identical or similar trade of goods or provision of 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;
 - (d) directly or indirectly results in bid rigging or collusive bidding, shall be presumed to have an appreciable adverse effect on competition:

Provided that nothing contained in this sub-section shall apply to any agreement entered into by way of joint ventures if such agreement increases efficiency in production, supply, distribution, storage, acquisition or control of goods or provision of services.

Explanation : For the purposes of this sub-section, “bid rigging” means any agreement, between enterprises or persons referred to in sub-section (3) engaged in identical or similar production or trading of goods or provision of services, which has the effect of eliminating or reducing competition for bids or adversely affecting or manipulating the process for bidding.

- (4) 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 arrangement;
 - (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.

Explanation : For the purposes of this sub-section,—

- (a) “Tie-in arrangement” includes any agreement requiring a purchaser of goods, as a condition of such purchase, to purchase some other goods;
- (b) “Exclusive supply agreement” includes any agreement restricting in any manner the purchaser in the course of his trade from acquiring or otherwise dealing in any goods other than those of the seller or any other person;
- (c) “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;
- (d) “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;
- (e) “Resale price maintenance” includes any agreement to sell goods on condition that the prices to be charged on the 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.



- (5) Nothing contained in this section shall restrict—
- (i) 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;
 - (ii) The right of any person to export goods from India to the extent to which the agreement relates exclusively to the production, supply, distribution or control of goods or provision of services for such export.

Abuse of dominant position

4. (1) No enterprise shall abuse its dominant position.
- (2) There shall be an abuse of dominant position under sub-section (1), if an enterprise or a group.—
- (a) directly or indirectly, imposes unfair or discriminatory—
 - (i) Condition in purchase or sale of goods or service; or
 - (ii) Price in purchase or sale (including predatory price) of goods or service,

Explanation : For the purposes of this clause, the unfair or discriminatory condition in purchase or sale of goods or service referred to in sub-clause (i) and unfair or discriminatory price in purchase or sale of goods (including predatory price) or service referred to in sub-clause (ii) shall not include such discriminatory condition or price which may be adopted to meet the competition; Or

- (b) limits or restricts—
 - (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; or
- (c) indulges in practice or practices resulting in denial of market access; or
- (d) 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; or
- (e) uses its dominant position in one relevant market to enter into, or protect, other relevant market.

Explanation : For the purposes of this section, the expression—

- (a) “dominant position” means a position of strength, enjoyed by an enterprise, 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;
- (b) “predatory price” means 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 the goods or provision of services, with a view to reduce competition or eliminate the competitors.
- (c) “group” shall have the same meaning as assigned to it in clause (b) of the Explanation to section 5.

Regulation of combinations :

Combination (Sec. 5)

5. The acquisition of one or more enterprises by one or more persons 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 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 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 of 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 rupees fifteen hundred crores in India;



Explanation : For the purposes of this section,—

- (a) “control” 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;
- (b) “group” means two or more enterprises which, directly or indirectly, are in a position to —
 - (i) exercise twenty-six per cent. or more of the voting rights in the other enterprise; or
 - (ii) appoint more than fifty percent, of the members of the board of directors in the other enterprise; or
 - (iii) control the management or affairs of the other enterprise;
- (c) the value of assets shall be determined by taking the book value of the 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, as reduced by any depreciation, and the value of assets shall include the brand value, value of goodwill, or value of copyright, patent, permitted use, collective mark, registered proprietor, registered trade mark, registered user, homonymous geographical indication, geographical indications, design or layout-design or similar other commercial rights, if any, referred to in sub-section (5) of section 3.

Regulation of combinations

6. (1) No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.
- (2) Subject to the provisions contained in sub-section (1), any person or enterprise, who or which proposes to enter into a combination, shall, at his or its option, 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—
 - (a) approval of the proposal relating to merger or amalgamation, referred to in clause (c) of section 5, by the board of directors of the enterprises concerned with such merger or amalgamation, as the case may be;
 - (b) execution of any agreement or other document for acquisition referred to in clause (a) of section 5 or acquiring of control referred to in clause (h) of that section.
- (2A) No combination shall come into effect until two hundred and ten days have passed from the day on which the notice has been given to the Commission under sub-section (2) or the Commission has passed orders under section 31, whichever is earlier.
- (3) The Commission shall, after receipt of notice under sub-section (2), deal with such notice in accordance with the provisions contained in sections 29, 30 and 31.
- (4) The provisions of this section shall 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.
- (5) The public financial institution, foreign institutional investor, bank or venture capital fund, referred to in sub-section (4) shall, within seven days from the date of the acquisition, file, in the form as may be specified by regulations, with the Commission the details of the acquisition including the details of control, the circumstances for exercise of such control and the consequences of default arising out of such loan agreement or investment agreement, as the case may be.

Explanation.—For the purposes of this section, the expression—

- (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(43 of 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(43 of 1961);



COMPETITION COMMISSION OF INDIA (CCI)

Establishment of Commission (Sec. 7)

7. (1) With effect from such date as the Central Government may, by notification, appoint, there shall be established, for the purposes of this Act, a Commission to be called the "Competition Commission of India".
- (2) The Commission shall be a body corporate by the name aforesaid having perpetual succession and a common seal with power, subject to the provisions of this Act, to acquire, hold and dispose of property, both movable and immovable, and to contract and shall, by the said name, sue or be sued,
- (3) The head office of the Commission shall be at such place as the Central Government may decide from time to time.
- (4) The Commission may establish offices at other places in India.

Composition of Commission (Sec. 8)

8. (1) The Commission shall consist of a Chairperson and not less than two and not more than six other Members to be appointed by the Central Government:
- (2) The Chairperson and every other Member shall be a 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 is in the opinion of the Central Government, may be useful to the Commission.
- (3) The Chairperson and other Members shall be whole-time Members.

Selection Committee for Chairperson and Members of Commission (Sec. 9)

9. (1) 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 –
- | | |
|--|----------------|
| (a) the Chief Justice of India or his nominee | - Chairperson; |
| (b) the Secretary, in the Ministry of Corporate Affairs | - Member; |
| (c) the Secretary in the Ministry of Law and Justice | - Member; |
| (d) 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. | - Member |
- (2) The term of the Selection Committee and the manner of selection of panel of names shall be such as may be prescribed.

Term of office of Chairperson and other Members (Sec. 10)

10. (1) 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 reappointment:
- Provided that the Chairperson or other Members shall not hold office as such after he has attained the age of sixty five years.
- (2) 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.
- (3) 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.
- (4) 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.



- (5) 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, removal and suspension of Chairperson and other members (Sec. 11)

11. (1) The Chairperson or any other Member may, by notice in writing under his hand addressed to the Central Government, resign his office:

Provided that the Chairperson or a Member 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.

- (2) Notwithstanding anything contained in sub-section (1), the Central Government may, by order, remove the Chairperson or any other Member from his office if such Chairperson 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 is 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.
- (3) Notwithstanding anything contained in sub-section (2), no Member shall be removed from his office on the ground specified in clause (d) or clause (e) of that subsection unless the Supreme Court, on a reference being made to it in this behalf by the Central Government, has, on an inquiry, held by it in accordance with such procedure as may be prescribed in this behalf by the Supreme Court, reported that the Member, ought on such ground or grounds to be removed.

Restriction on employment of Chairperson and other Members in certain cases (Sec. 12)

12. The Chairperson and other Members 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 Commission under this Act:

Provided that 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.

Administrative powers of Chairperson (Sec. 13)

13. The Chairperson shall have the powers of general superintendence, direction and control in respect of all administrative matters of the Commission:

Provided that the Chairperson may delegate such of his powers relating to administrative matters of the Commission, as he may think fit, to any other Member or officer of the Commission.

Salary and allowances and other terms and conditions of service of Chairperson and other Members (Sec. 14)

14. (1) The salary, and the other terms and conditions of service, of the Chairperson and other Members, including travelling expenses, house rent allowance and conveyance facilities, sumptuary allowance and medical facilities shall be such as may be prescribed.
- (2) The salary, allowances and other terms and conditions of service of the Chairperson or a Member shall not be varied to his disadvantage after appointment.



Vacancy, etc. not to invalidate proceedings of Commission

- 15.** No act or proceeding of the Commission shall be invalid merely by reason of—
- (a) any vacancy in, or any defect in the constitution of, the Commission; or
 - (b) any defect in the appointment of a person acting as a Chairperson or as a Member; or
 - (c) any irregularity in the procedure of the Commission not affecting the merits of the case.

Appointment of Director General, etc. (Sec. 16)

- 16.** (1) The Central Government may, by notification, appoint a Director General for the purposes of assisting the Commission in conducting inquiry into contravention of any of the provisions of this Act and for performing such other functions as are, or may be, provided by or under this Act.
- (1A) The number of other Additional, Joint, Deputy or Assistant Directors General or such officers or other employees in the office of Director General and the manner of appointment of such Additional, Joint, Deputy or Assistant Directors General or such officers or other employees shall be such as may be prescribed.
- (2) Every Additional, Joint, Deputy and Assistant Directors General or such officers or other employees shall exercise his powers, and discharge his functions, subject to the general control, supervision and direction of the Director General.
- (3) The salary, allowances and other terms and conditions of service of the Director General and Additional, Joint, Deputy and Assistant Directors General or such officers or other employees, shall be such as may be prescribed.
- (4) The Director General and Additional, Joint, Deputy and Assistant Directors General or such officers or other employees shall be appointed from amongst 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.

Appointment of Secretary, experts, professionals and officers and other employees of Commission (Sec. 17)

- 17.** (1) The Commission may appoint a Secretary and such officers and other employees as it considers necessary for the efficient performance of its functions under this Act.
- (2) The salaries and allowances payable to and other terms and conditions of service of the Secretary and officers and other employees of the Commission and the number of such officers and other employees shall be such as may be prescribed.
- (3) 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 this Act.

DUTIES, POWERS AND FUNCTIONS OF COMMISSION

Duties of Commission (Sec. 18)

- 18.** Subject to the provisions of this Act, it shall be the duty of the Commission to eliminate practices having adverse effect on competition, promote and sustain competition, protect the interests of consumers and ensure freedom of trade carried on by other participants, in markets in India: Provided that the Commission may, for the purpose of discharging its duties or performing its functions under this Act, enter into any memorandum or arrangement with the prior approval of the Central Government, with any agency of any foreign country.

Inquiry into certain agreements and dominant position of enterprise (Sec. 19)

- 19.** (1) The Commission may inquire into any alleged contravention of the provisions contained in subsection (1) of section 3 or sub-section (1) of section 4 either on its own motion or on—
- (a) receipt of any information, in such manner and accompanied by such fee as may be determined by regulations, from any person, consumer or their association or trade association; or



- (b) A reference made to it by the Central Government or a State Government or a statutory authority.
- (2) Without prejudice to the provisions contained in sub-section (1), the powers and functions of the Commission shall include the powers and functions specified in sub-sections (3) to (7).
- (3) The Commission shall, while determining whether an agreement has an appreciable adverse effect on competition under section 3, have 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.
- (4) The Commission shall, while inquiring whether an enterprise enjoys a dominant position or not under section 4, 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.
- (5) For determining whether a market constitutes a “relevant market” for the purposes of this Act, the Commission shall have due regard to the “relevant geographic market” and “relevant product market”.
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- (6) The Commission shall, while determining the “relevant geographic market”, 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 or regular supplies or rapid after-sales services.
- (7) The Commission shall, while determining the “relevant product market”, 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 specialised producers;
- (f) classification of industrial products.

Inquiry into combination by Commission (Sec. 20)

20. (1) The Commission may, upon its own knowledge or information relating to acquisition referred to in clause (a) of section 5 or acquiring of control referred to in clause (b) of section 5 or merger or amalgamation referred to in clause (c) of that section, inquire into whether such a combination has caused or is likely to cause an appreciable adverse effect on competition in India:

Provided that the Commission shall not initiate any inquiry under this sub-section after the expiry of one year from the date on which such combination has taken effect.

- (2) The Commission shall, on receipt of a notice under sub-section (2) of section 6, inquire whether a combination referred to in that notice or reference has caused or is likely to cause an appreciable adverse effect on competition in India.
- (3) Notwithstanding anything contained in section 5, the Central Government shall, on the expiry of a period of two years from the date of commencement of this Act and thereafter every two years, in consultation with the Commission, by notification, enhance or reduce, on the basis of the wholesale price index or fluctuations in exchange rate of rupee or foreign currencies, the value of assets or the value of turnover, for the purposes of that section.
- (4) For the purposes of determining whether a combination would have the effect of or is likely to have an appreciable adverse effect on competition in the relevant market, the Commission shall have due regard to all or any of the following factors, 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.

Reference by Statutory Authority

21. (1) Where in the course of a proceeding before any statutory Authority an issue is raised by any party that any decision which such statutory authority has taken or proposes to take is or would be, contrary to any of the provisions of this Act, then such statutory authority may make a reference in respect of such issue to the Commission:



Provided that any statutory authority, may suo moto make such a reference to the Commission.

- (2) On receipt of a reference under sub-section (1), the Commission shall give its opinion, within sixty days of receipt of such reference, to such statutory authority which shall consider the opinion of the Commission and thereafter, give its findings recording reasons therefor on the issues referred to in the said opinion.

Reference by Commission

- 21A.** (1) Where in the course of a proceeding before the Commission an issue is raised by any party that any decision which, the Commission has taken during such proceeding or proposes to take, is or would be, contrary to any of the provisions of this Act, whose implementation is entrusted to a statutory authority, then the Commission may make a reference in respect of such issue to the statutory authority:

Provided that the Commission, may suo moto make such a reference to the statutory authority.

- (2) On receipt of a reference under sub-section (1), the statutory authority shall give its opinion, within sixty days of receipt of such reference, to the Commission which shall consider the opinion of the statutory authority, and thereafter, give its findings recording reasons therefor on the issues referred to in the said opinion.

Meetings of Commission

- 22.** (1) 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.

- (2) 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.

- (3) 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 any equality of votes, the Chairperson or in his absence, the Member presiding, shall have a second or/casting vote.

Provided that the quorum for such meeting shall be three Members.

23, 24 and 25–Omitted by the Competition (Amendment) Act, 2007.

Procedure for inquiry under Section 19

- 26.** (1) On receipt of a reference from the Central Government or a State Government or a statutory authority or on its own knowledge or information received under section 19, if the Commission is of the opinion that there exists a prima facie case, it shall direct the Director General to cause an investigation to be made into the matter.

Provided that if the subject matter of an information received is, in the opinion of the Commission, substantially the same as or has been covered by any previous information received, then the new information may be clubbed with the previous information.

- (2) Where on receipt of a reference from the Central Government or a State Government or a statutory authority or information received under section 19, the Commission is of the opinion that there exists no prima facie case, it shall close the matter forthwith and pass such orders as it deems fit and send a copy of its order to the Central Government or the States Government or the statutory authority or the parties concerned, as the case may be.

- (3) The Director General shall, on receipt of direction under sub-section (1), submit a report on his findings within such period as may be specified by the Commission.

- (4) The Commission may forward a copy of the report referred to in sub-section (3) to the parties concerned; Provided that in case the investigation is caused to be made based on the reference received from the Central Government or the State Government or the statutory authority, the Commission shall forward a copy of the report referred in sub-section (3) to the Central Government or the State Government or the statutory authority, as the case may be.

- (5) If the report of the Director General referred to in sub-section (3) recommends that there is no contravention of the provisions of this Act, the Commission shall invite objections or suggestions from the Central Government or the State Government or the statutory authority, or the parties concerned, as the case may be, on such report of the Director General.



- (6) If, after consideration of the objections and suggestions referred to in sub-section (5), if any, the Commission agrees with the recommendation of the Director General, it shall close the matter forthwith and pass such orders as it deems fit and communicate its order to the Central Government or the State Government or the statutory authority or the parties concerned as the case may be.
- (7) If, after consideration of the objections or suggestions referred to in sub-section (5), if any, the Commission is of the opinion that further investigations is called for, it may direct further investigation in the matter by the Director General or cause further inquiry to be made by, in the matter or itself proceed with further inquiry in the matter in accordance with the provisions of this Act.
- (8) If the report of the Director General referred to in sub-section (3) recommends that there is contravention of any of the provisions of this Act, and the Commission is of the opinion that further inquiry is called for, it shall inquire into such contravention in accordance with the provisions of this Act.

Orders by Commission after inquiry into agreements or abuse of dominant position

27. Where after inquiry the Commission finds that any agreement referred to in section 3 or action of an enterprise in a dominant position, is in contravention of section 3 or section 4, as the case may be, it may pass all or any of the following orders, namely:—

- (a) direct any enterprise or association of enterprises or person or association of persons, as the case may be, involved in such agreement, or abuse of dominant position, to discontinue and not to re-enter such agreement or discontinue such abuse of dominant position, as the case may be;
- (b) impose such penalty, as it may deem fit which shall be not more than ten per cent of the average of the turnover for the last three preceding financial years, upon each of such person or enterprises which are parties to such agreements or abuse:

Provided that in case any agreement referred to in section 3 has been entered into by a cartel, the Commission may impose upon each producer, seller, distributor, trader or service provider included in that cartel, a penalty of upto three times of its profit for each year of the continuance of such agreement or ten percent of its turn over for each year of the continuance of such agreement, whichever is higher;

- (c) direct that the agreements shall stand modified to the extent and in the manner as may be specified in the order by the Commission;
- (d) direct the enterprises concerned to abide by such other orders as the Commission may pass and comply with the directions, including payment of costs, if any;
- (e) pass such other order or issue such directions as it may deem fit.

Provided that while passing orders under this section, if the Commission comes to a finding, that an enterprise in contravention to section 3 or section 4 of the Act is a member of a group as defined in clause (b) of the Explanation to section 5 of the Act, and other members of such a group are also responsible for, or have contributed to, such a contravention, then it may pass orders, under this section, against such members of the group.

Division of enterprise enjoying dominant position

28. (1) The Commission, on recommendation under clause (f) of section 27, 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 does not abuse its dominant position.

(2) In particular, and without prejudice to the generality of the foregoing powers, the order referred to in sub-section (1) 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.



- (3) Notwithstanding anything contained in any other law for the time being in force or in any contract or in any memorandum or articles of association, an officer of a company who ceases to hold office as such in consequence of the division of an enterprise shall not be entitled to claim any compensation for such cesser.

Procedure for investigation of combination

- 29.** (1) Where the Commission is of the 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, it shall issue a notice to show cause to the parties to combination calling upon them to respond within thirty days of the receipt of the notice, as to why investigation in respect of such combination should not be conducted.
- 1(A) After receipt of the response of the parties to the combination under sub-section(1), the Commission may call for a report from the Director General and such report shall be submitted by the Director General within such time as the Commission may direct.
- (2) The Commission, if it is prima facie of the opinion that the combination has, or is likely to have, an appreciable adverse effect on competition, it shall, within seven working days from the date of receipt of the response of the parties to the combination, direct the parties to the said combination to publish details of the combination within ten working days of such direction, in such manner, as it thinks appropriate, for bringing the combination to the knowledge or information of the public and persons affected or likely to be affected by such combination, or the receipt of the report from Director General called under sub section (1A), whichever is later direct the parties to the said combination to publish details of the combination within ten working days of such direction, in such manner, as it thinks appropriate, for bringing the combination to the knowledge or information of the public and persons affected or likely to be affected by such combination.
- (3) The Commission may invite any person or member of the public, affected or likely to be affected by the said combination, to file his written objections, if any, before the Commission within fifteen working days from the date on which the details of the combination were published under sub-section (2).
- (4) The Commission may, within fifteen working days from the expiry of the period specified in sub-section (3), call for such additional or other information as it may deem fit from the parties to the said combination.
- (5) The additional or other information called for by the Commission shall be furnished by the parties referred to in sub-section (4) within fifteen days from the expiry of the period specified in sub-section (4).
- (6) After receipt of all information and within a period of forty-five working days from the expiry of the period specified in sub-section (5), the Commission shall proceed to deal with the case in accordance with the provisions contained in section 31.

Procedure in case of notice under sub-section (2) of section 6

- 30.** Where any person or enterprises has given a notice under sub-section (2) of section 6. The Commission examine such notice and form its prima facie opinion as provided in sub-section (1) of section 29 and proceed as per provisions contained in that section.

Orders of Commission on certain combinations

- 31.** (1) Where the Commission is of the opinion that any combination does not, or is not likely to, have an appreciable adverse effect on competition, it shall, by order, approve that combination including the combination in respect of which a notice has been given under sub-section (2) of section 6.
- (2) Where the Commission is of the opinion that the combination has, or is likely to have, an appreciable adverse effect on competition, it shall direct that the combination shall not take effect.
- (3) Where the Commission is of the opinion that the combination has, or is likely to have, an appreciable adverse effect on competition but such adverse effect can be eliminated by suitable modification to such combination, it may propose appropriate modification to the combination, to the parties to such combination.
- (4) The parties, who accept the modification proposed by the Commission under sub-section (3), shall carry out such modification within the period specified by the Commission.



- (5) If the parties to the combination, who have accepted the modification under sub-section (4), fail to carry out the modification within the period specified by the Commission, such combination shall be deemed to have an appreciable adverse effect on competition and the Commission shall deal with such combination in accordance with the provisions of this Act.
- (6) If the parties to the combination do not accept the modification proposed by the Commission under sub-section (3), such parties may, within thirty working days of the modification proposed by the Commission, submit amendment to the modification proposed by the Commission under that sub-section.
- (7) If the Commission agrees with the amendment submitted by the parties under subsection (6), it shall, by order, approve the combination.
- (8) If the Commission does not accept the amendment submitted under sub-section (6), then, the parties shall be allowed a further period of thirty working days within which such parties shall accept the modification proposed by the Commission under sub-section (3).
- (9) If the parties fail to accept the modification proposed by the Commission within thirty working days referred to in sub-section (6) or within a further period of thirty working days referred to in sub-section (8), the combination shall be deemed to have an appreciable adverse effect on competition and be dealt with in accordance with the provisions of this Act.
- (10) Where the Commission has directed under sub-section (2) that the combination shall not take effect or the combination is deemed to have an appreciable adverse effect on competition under sub-section (9), then, without prejudice to any penalty which may be imposed or any prosecution which may be initiated under this Act, the Commission may order that—
 - (a) the acquisition referred to in clause (a) of section 5; or
 - (b) the acquiring of control referred to in clause (b) of section 5; or
 - (c) the merger or amalgamation referred to in clause (c) of section 5, shall not be given effect to: Provided that the Commission may, if it considers appropriate, frame a scheme to implement its order under this sub-section.
- (11) If the Commission does not, on the expiry of a period of two hundred and ten days from the date of notice given to the Commission under sub-section (2) of section 6, pass an order or issue direction in accordance with the provisions of sub-section (1) or sub-section (2) or subsection (7), the combination shall be deemed to have been approved by the Commission.

Explanation : For the purposes of determining the period of ninety working days specified in this subsection, the period of two hundred and ten days specified in sub-section (6) and a further period of thirty working days specified in sub-section (8) shall be excluded.

- (12) Where any extension of time is sought by the parties to the combination, the period of ninety working days shall be reckoned after deducting the extended time granted at the request of the parties.
- (13) Where the Commission has ordered a combination to be void, the acquisition or acquiring of control or merger or amalgamation referred to in section 5, shall be dealt with by the 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.
- (14) Nothing contained in this Chapter shall affect any proceeding initiated or which may be initiated under any other law for the time being in force.

Acts taking place outside India but having an effect on competition in India

32. The Commission shall, 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, have power to inquire into such agreement or abuse of dominant position or combination if such agreement or dominant position or combination has, or is likely to have, an appreciable adverse effect on competition in the relevant market in India.

have power to inquire in accordance with the provisions contained in sections 19, 20, 26, 29 and 30 of the Act into such agreement or abuse of dominant position or combination if such agreement or dominant position or combination has, or is likely to have, an appreciable adverse effect on competition in the relevant market in India and pass such orders as it may deem fit in accordance with the provisions of this Act.

Power to issue interim orders

- 33.** Where during an inquiry, the Commission is satisfied that an act in contravention of sub-section (1) of section 4 or section 6 has been committed and continues to be committed or that such act is about to be committed, the Commission may, by order, temporarily restrain any party from carrying on such act until the conclusion of such inquiry or until further orders, without giving notice to such party, where it deems it necessary.
- 34.** Omitted by competition (Amendment) Act, 2007.

Appearance before Commission

- 35.** A person or an enterprise or the Director General may either appear in person or authorise one or more chartered accountants or company secretaries or cost accountants or legal practitioners or any of his or its officers to present his or its case before the Commission.

Explanation : For the purposes of this section,—

- (a) “chartered accountant” means a chartered accountant as defined in clause (b) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 (38 of 1949) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;
- (b) “company secretary” means a company secretary as defined in clause (c) of sub-section (1) of section 2 of the Company Secretaries Act, 1980 (56 of 1980) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;
- (c) “cost accountant” means a cost accountant as defined in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 (23 of 1959) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;
- (d) “legal practitioner” means an advocate, vakil or an attorney of any High Court, and includes a pleader in practice.

Power of Commission to regulate its own procedure

- 36.** (1) In the discharge of its functions, the Commission shall be guided by the principals of natural justice and, subject to the other provisions of this Act and of any rules made by the Central Government, the Commission shall have the powers to regulate its own procedure.
- (2) The Commission 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, 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) requisitioning, subject to the provisions of sections 123 and 124 of the Indian Evidence Act, 1872, any public record or document or copy of such record or document from any office;
- (3) The Commission may call upon such experts, from the fields of economics, commerce, accountancy, international trade or from any other discipline as it deems necessary, to assist the Commission in the conduct of any inquiry by it.



(4) The Commission may direct any person—

- (a) to produce before the Director General or the Secretary or an officer authorised 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 this Act;
- (b) to furnish to the Director General or the Secretary or any officer authorised 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 this Act.

37. Omitted by competition (Amendment) Act, 2007.

Rectification of orders

38. (1) With a view to rectifying any mistake apparent from the record, the Commission may amend any order passed by it under the provisions of this Act.

(2) Subject to the other provisions of this Act, the Commission may make—

- (a) an amendment under sub-section (1) of its own motion;
- (b) an amendment for rectifying any such mistake which has been brought to its notice by any party to the order.

Explanation : For the removal of doubts, it is hereby declared that the Commission shall not, while rectifying any mistake apparent from record, amend substantive part of its order passed under the provisions of this Act.

Execution of orders of Commission imposing monetary penalty

39. (1) If a person fails to pay any monetary penalty imposed on him under this Act, the Commission shall proceed to recover such penalty, in such manner as may be specified by the regulations.

(2) In the case where the Commission is of the opinion that it would be expedient to recover the penalty imposed under this 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.

(3) 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 thereunder 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 and to the Commission instead of the Assessing Officer.

Explanation : Any reference to sub-section (2) or sub-section (6) of section 220 of the income tax Act, 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 XVIII 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.

40. Omitted by competition (Amendment) Act, 2007.



DUTIES OF DIRECTOR GENERAL

Director General to investigate contravention

- 41.** (1) The Director General shall, when so directed by the Commission, assist the Commission in investigating into any contravention of the provisions of this Act or any rules or regulations made thereunder.
- (2) The Director General shall have all the powers as are conferred upon the Commission under subsection (2) of section 36.
- (3) Without prejudice to the provisions of sub-section (2), 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 any other person investigating under his authority, as they apply to an inspector appointed under that Act.

Explanation : For the purposes of this section, -

- (a) the words 'the Central Government' under section 240 of the Companies Act, 1956 shall be construed as "the Commission";
- (b) the word "Magistrate" under section 240A of the Companies Act, 1956 shall be construed as "the Chief Metropolitan Magistrate, Delhi".

PENALTIES

Contravention of orders of Commission

- 42.** (1) The Commission may cause an inquiry to be made into compliance of its orders or directions made in exercise of its powers under the Act.
- (2) If any person, without reasonable clause, fails to comply with the orders or directions of the Commission issued under sections 27, 28, 31, 32, 33, 42A and 43A of the Act, he shall be punishable with fine which may extend to rupees one lakh for each day during which such non-compliance occurs subject to a maximum of rupees ten crores, as the Commission may determine.
- (3) If any person does not comply with the orders or directions issued, or fails to pay the fine imposed under sub-section (2), he shall, without prejudice to any proceeding under section 39, be punishable with imprisonment for a term which may extend to three years, or with fine which may extend to rupees twenty five crore, or with both, as the Chief Metropolitan Magistrate, Delhi may deem fit:
- Provided that the Chief Metropolitan Magistrate, Delhi shall not take cognizance of any offence under this section save on a complaint filed by the Commission or any of its officers authorised by it.

Compensation in case of contravention of orders of Commission

- 42A.** 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

- 43.** If any person fails to comply, without reasonable cause, with a direction given by—
- (a) the Commission under sub-sections (2) and (4) of section 36; or
- (b) 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 combinations

- 43A.** 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.



Penalty for making false statement or omission to furnish material information

44. If any person, being a party to a combination,—

- (a) makes a statement which is false in any material particular, or knowing it to be false; or
- (b) 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.

Penalty for offences in relation to furnishing of information

45. (1) Without prejudice to the provisions of section 44, if a person, who furnishes or is required to furnish under this Act any particulars, documents or any information,—

- (a) makes any statement or furnishes any document which he knows or has reason to believe to be false in any material particular; or
- (b) omits to state any material fact knowing it to be material; or
- (c) willfully alters, suppresses or destroys any document which is required to be furnished as aforesaid, such person shall be punishable with fine which may be extend to rupees one crore as may be determined by the Commission.

(2) Without prejudice to the provisions of sub-section (1), the Commission may also pass such other order as it deems fit.

Power to impose lesser penalty

46. The Commission may, if it is satisfied that 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 the alleged violations and such disclosure is vital, impose upon such producer, seller, distributor, trader or service provider a lesser penalty as it may deem fit, than leviable under this Act or the rules or the regulations:

Provided that lesser penalty shall not be imposed by the Commission in cases where the report of the investigation directed under section 26 has been received before making of such disclosure:

Provided further that lesser penalty shall be imposed by the Commission only in respect of a producer, seller, distributor, trader or service provider included in the cartel, who has made the full, true and vital disclosures under this section:

Provided also that lesser penalty shall not be imposed by the Commission if the person making the disclosure does not continue to cooperate with the Commission till the completion of the proceedings before the Commission:

Provided also that the Commission may, if it is satisfied that such producer, seller, distributor, trader or service provider included in the cartel had in the course of proceedings,—

- (a) not complied with the condition on which the lesser penalty was imposed by the Commission; or
- (b) had given false evidence; or
- (c) the disclosure made is not vital, and thereupon such producer, seller, distributor, trader or service provider may be tried for the offence with respect to which the lesser penalty was imposed and shall also be liable to the imposition of penalty to which such person has been liable, had lesser penalty not been imposed.

Crediting sums realised by way of penalties to Consolidated Fund of India

47. All sums realised by way of penalties under this Act shall be credited to the Consolidated Fund of India.

Contravention by companies

48. (1) Where a person committing contravention of any of the provisions of this Act or of any rule, regulation, order made or direction issued thereunder is 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, 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:



Provided that nothing contained in this sub-section shall render any such person liable to any punishment if he proves that the contravention was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such contravention.

- (2) Notwithstanding anything contained in sub-section (1), where a contravention of any of the provisions of this Act or of any rule, regulation, order made or direction issued thereunder has been committed by a company and it is proved that the contravention has taken place 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 contravention and shall be liable to be proceeded against and punished accordingly.

Explanation : For the purposes of this section,—

- (a) “Company” means a 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.

COMPETITION ADVOCACY

Competition advocacy

49. (1) The Central Government may, in formulating a policy on competition (including review of laws related to competition), or any other matter, and a State Government may, in formulating a policy on competition or on any other matter, as the case may be, make a reference to the Commission for its opinion on possible effect of such policy on competition and on receipt of such a reference, the Commission shall, within sixty days of making such reference, give its opinion to the Central Government or the State Government as the case may be, which may thereafter take further action as it deems fit.
- (2) The opinion given by the Commission under sub-section (1) shall not be binding upon the Central Government in formulating such policy.
- (3) The Commission shall take suitable measures for the promotion of competition advocacy, creating awareness and imparting training about competition issues.

FINANCE, ACCOUNTS AND AUDIT

Grants by Central Government

50. The Central Government may, after due appropriation made by Parliament by law in this behalf, make to the Commission grants of such sums of money as the Government may think fit for being utilised for the purposes of this Act.

Constitution of Fund

51. (1) There shall be constituted a fund to be called the “Competition Fund” and there shall be credited thereto—
- (a) All Government grants received by the Commission;
- (b) The fees received under this Act;
- (c) The interest accrued on the amounts referred to in clauses (a) and (c).
- (2) The Fund shall be applied for meeting—
- (a) the salaries and allowances payable to the Chairperson and other Members and the administrative expenses including the salaries, allowances and pension payable to the Director General, Additional, Joint, Deputy or Assistant Directors General, the Registrar and” officers and other employees of the Commission;
- (b) The other expenses of the Commission in connection with the discharge of its functions and for the purposes of this Act.
- (3) The Fund shall be administered by a committee of such Members of the Commission as may be determined by the Chairperson.
- (4) The committee appointed under sub-section (3) shall spend monies out of the Fund for carrying out the objects for which the Fund has been constituted.



Accounts and Audit

- 52.** (1) The Commission shall maintain proper accounts and other relevant records and prepare an annual statement of accounts in such form as may be prescribed by the Central Government in consultation with the Comptroller and Auditor-General of India.
- (2) The accounts of the Commission shall be audited by the Comptroller and Auditor-General of India at such intervals as may be specified by him and any expenditure incurred in connection with such audit shall be payable by the Commission to the Comptroller and Auditor-General of India.

Explanation : For the removal of doubts, it is hereby declared that the orders of the Commission, being matters appealable to the Appellate Tribunal or the Supreme Court, shall not be subject to audit under this section.

- (3) The Comptroller and Auditor-General of India and any other person appointed by him in connection with the audit of the accounts of the Commission shall have the same rights, privileges and authority in connection with such audit as the Comptroller and Auditor-General of India generally has, in connection with the audit of the Government accounts and, in particular, 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.
- (4) The accounts of the Commission as certified by the Comptroller and Auditor-General of India or any other person appointed by him in this behalf together with the audit report thereon shall be forwarded annually to the Central Government and that Government shall cause the same to be laid before each House of Parliament.

Furnishing of returns, etc., to Central Government

- 53.** (1) The Commission shall furnish to the Central Government at such time and in such form and manner as may be prescribed or as the Central Government may direct, such returns and statements and such particulars in regard to any proposed or existing measures for the promotion of competition advocacy, creating awareness and imparting training about competition issues, as the Central Government may, from time to time, require.
- (2) The Commission shall prepare once in every year, in such form and at such time as may be prescribed, an annual report giving a true and full account of its activities during the previous year and copies of the report shall be forwarded to the Central Government.
- (3) A copy of the report received under sub-section (2) shall be laid, as soon as may be after it is received, before each House of Parliament.

COMPETITION APPELLATE TRIBUNAL

Establishment of Appellate Tribunal:

- 53A.** (1) The Central Government shall, by notification, establish 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 subsection (2) of section 53Q of this Act, and pass orders for the recovery of compensation under section 53N of this Act.
- (2) The Headquarter of the Appellate Tribunal shall be at such place as the Central Government may, by notification, specify.



Appeal to Appellate Tribunal

- 53B.** (1) 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.
- (2) 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: Provided that 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.
- (3) 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.
- (4) The Appellate Tribunal shall send a copy of every order made by it to the Commission and the parties to the appeal.
- (5) 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

- 53C.** 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

- 53D.** (1) 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.
- (2) 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.

Selection Committee

- 53E.** (1) The Chairperson and members of the Appellate Tribunal 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 Chairperson;
 - the Secretary in the Ministry of Corporate Affairs..... Member;
 - the Secretary in the Ministry of Law and Justice Member.
- (2) The terms of the Selection Committee and the manner of selection of panel of names shall be such as may be prescribed.

Term of office of Chairperson and Members of Appellate Tribunal

- 53F.** 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: Provided that no Chairperson or other member of the Appellate Tribunal shall hold office as such after he has attained, –
- in the case of the Chairperson, the age of sixty-eight years;
 - in the case of any other member of the Appellate Tribunal, the age of sixty-five years.



Terms and conditions of service of chairperson and Members of Appellate Tribunal

53G(1) The salaries and allowances and other terms and conditions of service of the Chairperson and other members of the Appellate Tribunal shall be such as may be prescribed.

- (2) The salaries, allowances and other terms and conditions of service of the Chairperson and other members of the Appellate Tribunal shall not be varied to their disadvantage after their appointment.

Vacancies

53H. If, for any reason other than temporary absence, any vacancy occurs in the office of the Chairperson or a member of the Appellate Tribunal, the Central Government shall appoint another person in accordance with the provisions of this Act to fill the vacancy and the proceedings may be continued before the Appellate Tribunal from the stage at which the vacancy is filled.

Resignation of Chairperson and Members of Appellate Tribunal

53I. 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:

Provided that 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

53J.(1) 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.

- (2) 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.

Removal and suspension of Chairperson and Members of Appellate Tribunal

53K.(1) The Central Government may, in consultation with the Chief Justice of India, remove from office the Chairperson or any other member of the Appellate Tribunal, who-

- (a) has been adjudged an insolvent; or
 - (b) has engaged at any time, during his terms 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 become physically or mentally incapable of acting as such Chairperson or other Member of the Appellate Tribunal; or
 - (e) has acquired such financial or other interest as is likely to affect prejudicially his functions as such Chairperson or Member of the Appellate Tribunal; or
 - (f) has so abused his position as to render his continuance in office prejudicial to the public interest.
- (2) Notwithstanding anything contained in sub-section (1), no Chairperson or a Member of the Appellate Tribunal shall be removed from his office on the ground specified in clause (e) or clause (f) of sub-section (1) except by an order made by the Central Government after an inquiry made in this behalf by a Judge of the Supreme Court in which such Chairperson or member had been informed of the charges against him and given a reasonable opportunity of being heard in respect of those charges.

Restriction on employment of Chairperson and other Members of Appellate Tribunal in certain cases

53L. 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 this Act:



Provided that 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.

Staff of Appellate Tribunal

- 53M.** (1) The Central Government shall provide the Appellate Tribunal with such officers and other employees as it may think fit.
- (2) The officers and other employees of the Appellate Tribunal shall discharge their functions under the general superintendence and control of the Chairperson of the Appellate Tribunal.
- (3) The salaries and allowances and other conditions of service of the officers and other employees of the Appellate Tribunal shall be such as may be prescribed.

Awarding compensation

- 53N.** (1) 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.

- (2) 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.
- (3) 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:

Provided that the Appellate Tribunal may obtain the recommendations of the Commission before passing an order of compensation.

- (4) 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.

Explanation : For the removal of doubts, it is hereby declared that—

- (a) an application may be made for compensation before the Appellate Tribunal only after either the Commission or the Appellate Tribunal on appeal under clause (a) of sub-section(1) of section 53A of the Act, has determined in a proceeding before it that violation of the provisions of the Act has taken place, or if provisions of section 42A or sub-section(2) of section 53Q of the Act are attracted.
- (b) enquiry to be conducted under sub-section(3) shall be for the purpose of determining the eligibility and quantum of compensation due to a person applying for the same, and not for examining afresh the findings of the Commission or the Appellate Tribunal on whether any violation of the Act has taken place.

Procedures and powers of Appellate Tribunal

- 53O.** (1) The Appellate 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 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.

- (2) 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 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 (1 of 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.
- (3) 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 (45 of 1860) 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

- 53P.** (1) 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.
- (2) Notwithstanding anything contained in sub-section (1), 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

- 53Q.** (1) 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:
- Provided that 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.
- (2) 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.

Vacancy in Appellate Tribunal not to invalidate acts or proceedings

- 53R.** No act or proceeding of the Appellate Tribunal shall be questioned or shall be invalid merely on the ground of existence of any vacancy or defect in the constitution of the Appellate Tribunal.



Right to legal representation

- 53S.** (1) 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.
- (2) 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.
- (3) 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

- 53T.** 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;

Provided that 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

- 53U.** 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 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.

Power to exempt

- 54.** The Central Government may, by notification, exempt from the application of this Act, or any provision thereof, and for such period as it may specify in such notification—

- (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:

Provided that in case an enterprise is engaged in any activity including the activity relatable to the sovereign functions of the Government, the Central Government may grant exemption only in respect of activity relatable to the sovereign functions.

Power of Central Government to issue directions

- 55.** (1) Without prejudice to the foregoing provisions of this Act, the Commission shall, in exercise of its powers or the performance of its functions under this Act, be bound by such directions on questions of policy, other than those relating to technical and administrative matters, as the Central Government may give in writing to it from time to time:



Provided that the Commission shall, as far as practicable, be given an opportunity to express its views before any direction is given under this sub-section.

(2) The decision of the Central Government whether a question is one of policy or not shall be final.

Power of Central Government to supersede Commission

56. (1) If at any time the Central Government is of the opinion—

- (a) that on account of circumstances beyond the control of the Commission, it is unable to discharge the functions or perform the duties imposed on it by or under the provisions of this 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 the discharge of the functions or performance of the duties imposed on it by or under the provisions of this Act and as a result of such default the financial position of the Commission or the administration of the Commission has suffered; or
- (c) that circumstances exist which render it necessary in the public interest so to do, the Central Government may, by notification and for reasons to be specified therein, supersede the Commission for such period, not exceeding six months, as may be specified in the notification: Provided that before issuing any such notification, the Central Government shall give a reasonable opportunity to the Commission to make representations against the proposed supersession and shall consider representations, if any, of the Commission.

(2) Upon the publication of a notification under sub-section (1) superseding the Commission,—

- (a) The Chairperson and other Members shall 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 this Act, be exercised or discharged by or on behalf of the Commission shall, until the Commission is reconstituted under sub-section (3), be exercised and discharged by the Central Government or such authority as the Central Government may specify in their behalf;
 - (c) All properties owned or controlled by the Commission shall, until the Commission is reconstituted under sub-section (3), vest in the Central Government.
- (3) On or before the expiration of the period of supersession specified in the notification issued under subsection (1), the Central Government shall reconstitute the Commission by a fresh appointment of its Chairperson and other Members and in such case any person who had vacated his office under clause (a) of sub-section (2) shall not be deemed to be disqualified for re-appointment.
- (4) The Central Government shall cause a notification issued under sub-section (1) and a full report of any action taken under this section and the circumstances leading to such action to be laid before each House of Parliament at the earliest.

Restriction on disclosure of information

57. No information relating to any enterprise, being an information which has been obtained by or on behalf of the Commission or the Appellate Tribunal for the purposes of this Act, shall, without the previous permission in writing of the enterprise, be disclosed otherwise than in compliance with or for the purposes of this Act or any other law for the time being in force.

Chairperson, Members, Director General, Secretary, officers and other employees, etc. to be public servants

58. The Chairperson and other Members and the Director General, Additional, Joint, Deputy or Assistant Directors General and Secretary and officers and other employees of the Commission and the Chairperson, Members, officers and other employees of the Appellate Tribunal shall be deemed, while acting or purporting to act in pursuance of any of the provisions of this Act, to be public servants within the meaning of section 21 of the Indian Penal Code.

**Protection of action taken in good faith**

59. No suit, prosecution or other legal proceedings shall lie against the Central Government or Commission or any officer of the Central Government or the Chairperson or any Member or the Director-General, Additional, Joint, Deputy or Assistant Directors General or Secretary or officers or other employees of the Commission or the Chairperson, members, officers and other employees of the Appellate Tribunal for anything which is in good faith done or intended to be done under this Act or the rules or regulations made thereunder.

Act to have overriding effect

60. The provisions of this Act shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force.

Exclusion of jurisdiction of civil courts

61. No civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which the Commission or the Appellate Tribunal is empowered by or under this 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 this Act.

Application of other laws not barred

62. The provisions of this Act shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force.

Power to make rules

- 63.** (1) The Central Government may, by notification, make rules to carry out the provisions of this Act;
- (2) In particular, and without prejudice to the generality of the foregoing power, such rules may 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) 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;
 - (ca) the number of Additional, Joint, Deputy or Assistant Directors General or such officers or other employees in the office of Director General and the manner in which such Additional, Joint, Deputy or Assistant Directors General or such officers or other employees may be appointed under sub-section (1 A) of section 16;]
 - (d) the salary, allowances and other terms and conditions of service of the Director General, Additional, Joint, Deputy or Assistant Directors General or [93][such officers or other employees] under sub-section (3) of section 16;
 - (e) 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;
 - (f) the salaries and allowances and other terms and conditions of service of the [95][Secretary] and officers and other employees payable, and the number of such officers and employees under sub-section (2) of section 17;
 - (g) the form in which the annual statement of accounts shall be prepared under sub-section (1) of section 52;
 - (h) the time within which and the form and manner in which the Commission may furnish returns, statements and such particulars as the Central Government may require under sub-section (1) of section 53;



- (i) the form in which and the time within which the annual report shall be prepared under sub-section (2) of section 53;
 - (j) 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.
- (3) Every notification issued under sub-section(3) of section 20 and section 54 and every rule made under this Act by the Central Government 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 notification or rule, or both Houses agree that the notification should not be issued or rule should not be made, the notification or 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 notification or rule, as the case may be.

Power to make regulations

- 64.** (1) The Commission may, by notification, make regulations consistent with this Act and the rules made thereunder to carry out the purposes of this Act.
- (2) In particular, and without prejudice to the generality of the foregoing provisions, 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 the acquisition shall be filed under subsection(5) of Section 6;
 - (d) the procedures to be followed for engaging the experts and 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 the 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.
- (3) Every regulation made 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 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; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that regulation.

Power to remove difficulties

- 65.** (1) If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order published in the Official Gazette, make such provisions, not inconsistent with the provisions of this Act as may appear to it to be necessary for removing the difficulty :
- Provided that no such order shall be made under this section after the expiry of a period of two years from the commencement of this Act.
- (2) Every order made under this section shall be laid, as soon as may be after it is made, before each House of Parliament.



4.4 NEGOTIABLE INSTRUMENTS ACT, 1881

INTRODUCTION

Negotiable Instrument Act, 1881 primarily contains the law relating to negotiable instruments. The term 'negotiable' means transferable and the term 'instrument' means 'any written document creating a right in favour of some person.' Thus by negotiable instrument we mean a written document by which a right is given to a person and which is transferable in accordance with provisions of Negotiable Instrument Act, 1881.

Sec. 13 defines a negotiable instrument as 'a promissory note, bill of exchange or cheque payable either to order or to bearer.'

1.1. Characteristics of a Negotiable Instrument

- (1) Freely transferable- If a negotiable instrument is payable to bearer, it is transferred by mere delivery and if payable to order, then by endorsement and delivery.
- (2) Holder's title is free from all defects-A transferee taking a instrument bonafide and for value gets the instrument free from all defects in the title of the previous holder. The transferee is known as the holder in due course.
- (3) The holder in due course can sue on the instrument in his own name and for this purpose notice of transfer need not be given.
- (4) A negotiable instrument is subject to certain presumptions:
 - (a) *Consideration* :Every negotiable instrument is presumed to be made, accepted, endorsed, negotiated or transferred for certain consideration.
 - (b) *Date*: Every negotiable instrument bear the date on which it was drawn or made.
 - (c) *Time of acceptance*: Every negotiable instrument is deemed to have been accepted within a reasonable time after the date mentioned on it and before its maturity.
 - (d) *Time of transfer*: It is presumed to have been transferred before maturity.
 - (e) *Order of endorsements*: The endorsement made are deemed to have been made in the order they appear on the instrument.
 - (f) Every holder is presumed to be the holder in due course.
 - (g) In case an instrument is lost , it is presumed that the instrument was duly stamped.
 - (h) In case of dishonour of an instrument, if a suit is filed, the court shall on proof of protest presume the fact of dishonour, unless it is disproved.

1.2. Types of Negotiable Instrument

Negotiable Instruments are of two types :

- (1) **Negotiable by statute** - The Act mentions three kinds of negotiable instruments-promissory notes, bills of exchange, and cheques.
- (2) **Negotiable by custom or usage** - Certain other instruments takes the character of negotiable instruments by custom or usage-dividend warrant, share certificates, circular notes, bearer debentures are some of them.

2.1. Promissory Notes

A 'promissory note' is an instrument in writing (not being a bank note or currency note) containing an *unconditional* undertaking signed by maker , to pay a certain sum of money only to or to order of a certain person or to bearer of the instrument.(Sec.4). There are two parties to it -the maker and the payee.

For example, D signs an instrument stating, 'I promise to pay F or order ` 1000'.This is a promissory note.

Thus essential elements of a promissory note are :

- (i) Must be in writing.
- (ii) Must contain an express promise to pay.
- (iii) The promise must be definite and unconditional.



- (iv) It should be signed by maker.
- (v) The parties –maker & payee must be certain.
- (vi) The promise should be to pay certain sum of money only.
- (vii) Must bear necessary stamp as per Indian Stamp Act, 1899.
- (viii) It cannot be made payable to bearer on demand.

2.2. Bill of Exchange

A Bill of Exchange is an instrument in writing containing an unconditional order signed by 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 (Sec.5) There are three parties to a bill, namely drawer, drawee and payee.

A signs an instrument directing B 'Pay C or order a sum of ₹ 1000/- only, 3 months after date'. This is BOE.

Essential features of a bill of exchange are –

- (i) Must be in writing
- (ii) Must contain an unconditional order.
- (iii) The order must be to pay money only.
- (iv) The amount must be certain .
- (v) Requires three parties.
- (vi) The parties must be certain .
- (vii) It should be signed by drawer.
- (viii) Necessary stamp must be affixed.

2.3. Cheque

A cheque is a bill of exchange drawn on a specified banker payable on demand.(Sec.6) Further the expression includes the electronic image of a truncated cheque or a cheque in electronic form. All cheques are bills of exchange but all bills of exchange are not cheques. A cheque is required to possess all essential features of a bill of exchange. But a cheque does not require acceptance as it is intended for immediate payment.

Comparative analysis of Promissory Note, Bill of Exchange and Cheque.

Particulars	Promissory Note	Bill of Exchange	Cheque
Parties	2 parties-maker & payee	3 parties-drawer, drawee & payee	3 parties - drawer, banker, and payee
Nature	Contains an unconditional promise by maker to pay the payee	Contains an unconditional order to the drawee to pay the payee	Drawn on specified banker to pay on demand.
Acceptance	Not necessary	Necessary if the bill is payable after sight.	Not necessary.
Liability	Liability of maker is primary and absolute.	Liability of drawer is conditional and secondary upon nonpayment by drawee.	Liability of drawer is conditional and secondary upon nonpayment by banker
Notice of dishonour	Not necessary	Necessary	Not necessary
Payable	On demand or after a specified time. Cannot be made payable to bearer on demand or even after certain period.	On demand or after a specified time. Cannot be made payable to bearer on demand.	On demand even to bearer if so made.
Crossing	Not possible	Not possible	Can be crossed.

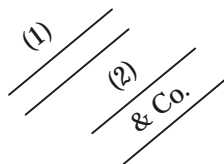


Particulars	Promissory Note	Bill of Exchange	Cheque
Noting and protesting in case of dishonour	Not required	Required to establish the fact of dishonour.	Not required.
Grace period	Available if payable after specified time	Available if payable after specified time (usance bill)	Not available.
Other features	Number, date, place not essential. Must be stamped.	Number, date, place not essential. Must be stamped.	Number, date, place, essential. Need not be stamped.

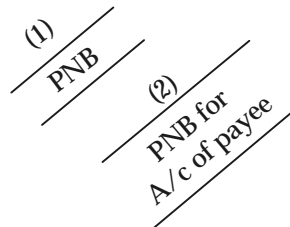
Crossing of Cheque

Cheques are of two types-open and crossed. When a cheque is payable in cash across the counter of a bank, it is said to be open. A crossed cheque is one on which two parallel transverse lines with or without the words '&Co.' are drawn. Crossing a cheque implies directing the drawee banker to pay the amount only to a banker or a particular banker so that the party getting payment can be easily traced. A cheque may be crossed by the drawer, holder, or banker. Crossing may be of two types –general and special. Specimens are shown below :

General Crossing



Special Crossing



Marking of cheques

Marking is writing on a cheque by drawee banker that it would be honoured when it is duly presented for payment. Cheques may be marked at the instance of the drawer, holder or collecting banker. In India no such practice of getting cheques marked has been established either by judicial decisions or by statutes.

2.4. Classification of Negotiable Instruments

(1) *Bearer and order instruments*

A negotiable instrument is said to be payable to bearer when (i) it is expressed to be so payable (ii) only or last endorsement is a blank endorsement.

A negotiable instrument is said to be payable to order when (i) it is expressed to be so payable (ii) expressed to be payable to a particular person with restricting its transferability.

(2) *Inland and foreign instruments*

A bill, promissory note or cheque if both drawn and payable in India or drawn on a person resident in India is said to be an inland bill.

A bill which is not an inland bill is deemed to be a foreign bill.

(3) *Demand and time instruments*

An instrument is payable on demand when it is expressed to be so payable or when no time is specified on it. A cheque is always payable on demand as discussed earlier.

A note or bill if payable after a specified period or happening of a specified event which is certain, it is a time instrument.



(4) *Genuine, accommodation and fictitious bill*

When a bill is drawn, accepted, or endorsed for consideration it is a genuine bill. When it is drawn, accepted, or endorsed without consideration it is accommodation bill. When drawer or payee or both are fictitious the bill is called fictitious bill.

(5) *Clean and documentary bill*

When no documents relating to goods are annexed to the bill, it is clean bill. When documents of title or other documents relating to goods are attached, it is documentary bill.

(6) *Ambiguous instrument*

When an instrument due to faulty drafting may be interpreted either as bill or note, it is an ambiguous instrument. It is for holder to decide how he wants the bill to be treated. Ambiguity may also arise when the amount is stated differently in words and figures. In such case the amount stated in words will be taken into account.

(7) *Inchoate instrument*

An instrument incomplete in some respect is known as inchoate instrument.

2.5. A bill of exchange drawn in parts is known as bill in sets. Each part should contain a reference to other parts. This type of bill is specially drawn when it is to be sent to some foreign country.

2.6. Due date of a bill or note

Every instrument payable, otherwise, than **on demand** is entitled to three days of grace. Instruments not entitled to 'period of grace' are :

- (i) a cheque
- (ii) a bill or note payable on demand,
- (iii) a bill or note in which no time is mentioned.

Instruments entitled to 'period of grace' are :

- (i) a bill or note payable on a specified day,
- (ii) a bill or note payable 'after sight',
- (iii) a bill or note payable at a certain period on happening of a certain event.

So in case of time bill or note, it becomes due on the last day of grace period. Where an instrument is payable by installments, each installment is due three days after the date fixed for payment of the installment. If the due date falls on a public holiday, the bill becomes due on immediate preceding business day. If the month in which the period is to terminate has no corresponding day, the period will terminate on the last day of the month.

Examples :

- (i) A bill dated 6th February, 2009 is made payable 90 days after date. Its due date is 9th May, 2009.
- (ii) A bill dated 1st January, 2009 is made payable one month after date. It falls due on 3rd March, 2009.
- (iii) A bill falls due on 9th May, 2009 which happens to be a Sunday. Then due date becomes 8th May, 2009.

2.7. Payment in due course

Payment in due course results in discharge of the instrument. A payment is said to be 'payment in due course' if it satisfies the following conditions :

- (i) It is in accordance with apparent tenor of the instrument.
- (ii) It is made on behalf of drawee or acceptor.
- (iii) It is made to the person in possession of the instrument and also entitled to payment.
- (iv) It is made in good faith, without negligence and under bonafide circumstances.
- (v) There is no ground for believing that possessor is not entitled to receive payment.



3.1. Capacity to become a party to a negotiable instrument

A person competent to contract can become a party to a negotiable instrument. If a party who makes, draws, endorses, or negotiates a negotiable instrument is incompetent to do so, the agreement is void as against him. But the contract is still valid against other the parties competent to contract. The following entities cannot bind themselves by becoming a party to a negotiable instrument :

- (i) a minor,
- (ii) a person of unsound mind,
- (iii) corporations beyond the powers conferred by memorandum and articles,
- (iv) an agent-general authority to transact business and to receive or discharge debts does not confer the right to accept or endorse bills or notes so as to bind the principal,
- (v) partner of a non trading firm unless expressly provided.

3.2. Holder(Sec 8) and Holder in due Course (Sec 9)

A holder of a negotiable instrument is a person who is entitled in his own name (i) to the possession of the instrument (ii) to receive or recover the amount thereon from the parties thereto.

Holder in due course is the person who becomes (i) the possessor of the negotiable instrument if payable to bearer or payee if payable to order for consideration (ii) becomes holder of the instrument before maturity (iii) obtains the instrument bonafide, i.e. in good faith without having reason to believe that there is defect in the title.

A holder of a negotiable instrument may not be holder in due course if –

- (i) he obtains the instrument without consideration or unlawful consideration or illegal means,
- (ii) he obtains the instrument after its maturity,
- (iii) he does not obtain the instrument bonafide.

Difference between holder and holder in due course

Holder	Holder in due course
(1) Holder is entitled in his own name to possess the instrument and the amount thereon from parties involved.	Holder in due course possesses the instrument for consideration before maturity and in good faith.
(2) Title of the holder is subject to title of the transferor.	Holder in due course gets a better title than transferor.
(3) Holder may receive the instrument without consideration.	Holder in due course always receives the instrument for consideration.
(4) Holder does not get certain privileges available to the holder in due course.	Holder in due course always gets privileges not available to holder.

Privileges available to holder in due course

- (i) A holder in due course can fill in an inchoate stamped instrument for any amount provided the stamp is sufficient to cover the amount.
- (ii) Every prior party to a negotiable instrument is liable to the holder in due course until the amount is fully satisfied.
- (iii) Acceptor of an instrument is liable to the holder in due course even if the other parties to the instrument are fictitious.
- (iv) A negotiable instrument drawn or accepted without consideration is void and creates no liability to pay. However if it falls into the hands of a holder in due course the acceptor can no longer deny payment.
- (v) If a bill or note is negotiated to a holder due course, payment cannot be denied on the ground that the instrument was made for specific purpose only.
- (vi) Once a negotiable instrument passes through the hands of a holder due course, all its defects get cleansed.



- (vii) The person liable on a negotiable instrument cannot defend himself on the pretext that the instrument was lost or obtained from him in a fraudulent manner.
- (viii) Validity of a negotiable instrument as originally made cannot be denied as against a holder in due course.
- (ix) No drawer or acceptor of an instrument is permitted to deny payee's capacity at the date of the note or bill, to endorse the same in a suit by a holder in due course.
- (x) The endorser cannot deny the signature or capacity to contract of any prior parties in a suit by a holder in due course.

4.1. Negotiation

An essential characteristic of a negotiable instrument is that it is freely transferable. The transfer may take place through (i) negotiation (ii) assignment.

Difference between negotiation and assignment

Negotiation	Assignment
(1) Negotiation may be effected by mere delivery if the instrument is bearer one or endorsement and delivery if it is an order instrument.	Assignment should always be on a written document signed by transferor.
(2) Transferee gets the rights of Holder in due course.	Title of the transferee is always subject to the title of the transferor.
(3) Consideration is always presumed.	Consideration must be proved.
(4) No information of transfer needs to be given to the debtor in order to bind him.	Notice of assignment is must in order to bind the debtor.

The Negotiable Instruments Act does not deal with transfer of negotiable instrument through assignment.

Transfer through negotiation takes place by two methods :

- (i) Bearer instruments – Negotiable by delivery only.
- (ii) Order instruments – Negotiable by endorsement and delivery.

4.2. Endorsement

Endorsement (Indorsement) means writing of a person's name (other than maker) on the face or back of an instrument or on a slip of paper attached thereto for the purpose of negotiation. The person signing the instrument is known as endorser and the person in whose favour it is endorsed is known as endorsee.

Essentials of a valid endorsement (indorsement)

- (1) It must be on the instrument itself or on a separate slip of paper (called allonge) attached thereto.
- (2) For the purpose of negotiation, it must be signed by the endorser.
- (3) The instrument may contain in addition to the signature of the endorser, the name of the endorsee also. No particular form of words is necessary for endorsement.
- (4) Endorsement is complete when the instrument is delivered to the endorsee with the intention of passing the property in it to the endorsee. Delivery is to be made by the endorser himself or someone on behalf of him.

5. Presentment of a negotiable instrument

Presentment of a negotiable instrument means showing the instrument to the drawer, acceptor, or maker for acceptance, sight or payment.



5.1. Presentment for acceptance – Only certain types of bills require acceptance. Essentials of a valid acceptance are—

- (i) Must be written on the face of the bill,
- (ii) The bill must be signed by drawee or his authorized agent.
- (iii) The accepted bill is required to be delivered to the holder of the instrument.

Modes of acceptance – (i) **General** - When no condition or qualification is attached to the acceptance, it is general.
 (ii) **Qualified**- When acceptance is subject to certain qualification.

5.2. Presentment for sight – In case of a note, question of acceptance doesnot arise as maker himself is primarily responsible for it. However if the note is payable at a certain period after sight, it must be presented to the maker for fixing its maturity.

5.3. Presentment for payment – A negotiable instrument should be presented for payment in order to hold the acceptor liable.

Presentment for payment not necessary in the following circumstances :

- (i) The drawer could not suffer damage for want of presentment.
- (ii) The bill is dishonoured by non-acceptance.
- (iii) The drawer is a fictitious person.
- (iv) The drawer and drawee are the same person.
- (v) The maker/acceptor intentionally prevents presentment of the instrument.
- (vi) If the instrument is payable at a specified place and the maker/acceptor is not present there at usual business hours.
- (vii) If the instrument is not payable at a specified place, and maker/acceptor could not be found after due search.
- (viii) Presentment is waived either expressly or impliedly by the party entitled to presentment before or after maturity of the bill or note.
- (ix) There is a promise to pay , notwithstanding non – presentment.
- (x) Presentment becomes impossible.

In all the above mentioned cases the instrument is deemed to be dishonoured on due date of presentment for payment if the payment is not received.

6. Dishonour of Negotiable Instrument

A bill may be dishonoured by non-acceptance or non-payment. A cheque or note is dishonoured by non-payment only. If an instrument is dishonoured, the holder must give notice of dishonour to all prior parties unless the notice is excused, otherwise he loses his right of action against all prior parties.

6.1. Object of Notice : Notice of dishonour is necessary to inform the prior parties liable on the instrument about liability which accrues as a result of dishonour of the instrument.

6.2. Form of Notice : Notice of dishonour may be oral or written. When written, it may be sent by post. It must be given within reasonable time at the place of business or residence (if there is no place of business) to the party for whom it is intended.

Reasonable time is depends on nature of instrument and usual course of dealing with respect to similar instruments.Public holidays are to be excluded in calculating time.

6.3. Notice of dishonour is not necessary in the following circumstances :

- (i) When it is dispensed with by the party entitled thereto.
- (ii) When the party charged could not suffer damage for want of notice.
- (iii) In case of a promissory note which is not negotiable.
- (iv) To charge the drawer when drawer and acceptor are the same person.



- (v) When the party entitled to notice , promises unconditionally to pay the amount due on the instrument.
- (vi) When the party entitled to notice could not be found after due search.
- (vii) To charge the drawee, when he has countermanded payment.

6.4. Duties of the holder upon dishonour

- (i) The holder must give notice of dishonour to all prior parties who are liable to pay.
- (ii) Upon dishonour of the instrument, the holder may get the fact of dishonour noted and protested by the Notary Public.
- (iii) After the formality of noting and protesting, the last option available to the holder is to file suit for the amount due against the parties liable for payment.

6.5. Instruments acquired after the notice of dishonour/maturity : Holder acquiring the instrument after notice of dishonour or after maturity, as against the other parties, has the rights of his immediate transferor.

6.6. Noting : Noting means recording the fact of dishonour by Notary Public upon the instrument. Noting must contain the following particulars :

- (i) the fact of dishonour,
- (ii) date of dishonour
- (iii) reasons, if any, assigned for dishonour,
- (iv) if the instruments is not expressly dishonoured, reasons why the holder thinks so,
- (v) Notary charges.

6.7. Protest : It is a formal notarial certificate attesting the dishonour of a bill or note. A protest must contain the following particulars :

- (i) the instrument or literal transcript of the same;
- (ii) the name of the person for whom or against whom the instrument is protested;
- (iii) the fact of dishonour;
- (iv) place and time of dishonour;
- (v) signature of the Notary Public;
- (vi) in case of acceptance/payment for honour, name of the person accepting or paying and the name of the person for whom it is paid or accepted.

6.8. Rules as to Compensation

1. Compensation to holder : The holder is entitled to receive-

- (i) the amount due on the instrument,
- (ii) expenses incurred in presenting, noting and protesting the instrument.

2. Re-exchange : Where the person charged resides in a country different from that in which the instrument was payable, the holder is entitled to receive the compensation at current rate of exchange between two countries on the date of dishonour.

3. Compensation to endorser : The endorser, who being liable has paid the amount due on the instrument is entitled to receive the amount along with interest @18%p.a. from the date of payment till realization of the amount together with the incidental expenses.

4. Re-draft : The party entitled to compensation may draw a bill for the amount due along with expenses incurred thereon. Such a bill is called 'redraft'. If redraft is dishonoured, the party dishonouring the same is liable to compensate in the same manner as in case of original bill.

6.9. Penalties in case of Dishonour of certain cheques for insufficiency offunds (Section 138 to 142)

Advent of cheques in the market have given a new dimension to the commercial and corporate world, its time when people have preferred to carry and execute a small piece of paper called Cheque than carrying the currency worth the value of cheque. Dealings in cheques are vital and important not only for banking



purposes but also for the commerce and industry and the economy of the country. But pursuant to the rise in dealings with cheques also rises the practice of giving cheques without any intention of honoring them. Before 1988 there being no effective legal provision to restrain people from issuing cheques without having sufficient funds in their account or any stringent provision to punish them in the event of such cheque not being honoured by their bankers and returned unpaid. Of course on dishonour of cheques there is a civil liability accrued. However in reality the processes to seek civil justice becomes notoriously dilatory and recover by way of a civil suit takes an inordinately long time. To ensure promptitude and remedy against defaulters and to ensure credibility of the holders of the negotiable instrument a criminal remedy of penalty was inserted in Negotiable Instruments Act, 1881 in form of the Banking, Public Financial Institutions and Negotiable Instruments Laws (Amendment) Act, 1988 which were further modified by the Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002[3].

1. Dishonour of cheque for insufficiency of funds in the account :

Section 138 creates statutory offence in the matter of dishonour of cheques on the ground of insufficiency of funds in the account maintained by a person with the banker. Section 138 of the Act can be said to be falling either in the acts which are not criminal in real sense, but are acts which in public interest are prohibited under the penalty or those where although the proceeding may be in criminal form, they are really only a summary mode of enforcing a civil right. Normally in criminal law existence of guilty intent is an essential ingredient of a crime. However the Legislature can always create an offence of absolute liability or strict liability where 'mens rea' is not at all necessary.

While elucidating on this aspect the Kerala High Court in *K. S. Auto v. Union of India* held that :

"Knowledge or reasonable belief, that pre requisite could be statutorily dispensed with in appropriate cases by creating strict liability offences in the interest of the Nation."

Further the creation of the strict liability is an effective measure by encouraging greater vigilance to prevent usual callous or otherwise attitude of drawers of cheques in discharge of debts or otherwise. The words as appearing in clause (b) of S. 138 cannot be construed even to imply failure without reasonable cause in view of the explicit language in which the provision is couched, the principle of strict liability incorporated in the main enacting clause.

2. Presumption in favour of the holder (sec 139)

It shall be presumed unless otherwise proved that the holder of a cheque has received the cheque for discharge in whole or in part of any debt or liability.

3. Defence which may not be allowed in any prosecution u/s 138 (sec140)

The drawer cannot pray that at the time of issue of cheque, he had no reason to believe that the cheque will be dishonoured.

4. Offences by Companies (sec.141)

In case the party committing an offence is a company, every person in charge of the company and responsible in carrying out the business, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. However the person will not be liable if-

- (i) it is proved that the offence was committed without his knowledge;
- (ii) where he has exercised all due diligence to prevent occurrence of that offence;
- (iii) where a person is Director as a Government nominee.

5. Cognizance of offences

- (i) No court inferior to that of a Metropolitan Magistrate or Judicial Magistrate of first class shall try any offence u/s 138.
- (ii) No court shall take cognizance of offences u/s 138 except upon a complaint, in writing made by payee or holder in due course.
- (iii) Such complaint should be made within one month from the date on which cause of action arises.
- (iv) The complainant may satisfy the court that there was sufficient ground for not making the complaint within such period.



Constitutional validity of the provisions

In **B. Mohana Krishna v. Union of India**, the question came up for consideration that whether the presumption raised in section 138 that the holder of the cheque received the cheque of the nature referred to in section 138, unless the contrary is established is violative of Article 20 (3) of the Constitution of India. The Court while answering negative held that:

“Unless a person is compelled to be a witness against himself Article 20 (3) has no application. The person charged under section 138 is not compelled to be a witness against himself. The presumption of the nature incorporated in section 139 is a common feature in criminal statutes for example section 12 of the Protection of Civil rights Act. The presumption under section 139 in favour of holder of cheque would not, therefore be violative of Article 20 (3).”

Further such imposition of strict liability was put to judicial scrutiny on grounds of unreasonableness and arbitrariness in **Mayuri Pulse Mills v. Union of India** where the Bombay High Court held that :

“Normally in Criminal law existence of a guilty intent is an essential ingredient of a crime and the principle is expressed in the maxim ‘actus non facit rum nisi mens sit rea’. This is a general principle. However the legislature can always create an offence of absolute liability or strict liability are justified and cannot be said to be unreasonable.”

Section 138 was also put to test in **Ramawati Sharma v. Union of India** in light of Article 21 of the Constitution of India where the court held that :

“Mere taking of loan is not, thus, made punishable under certain circumstances and after following certain conditions. It may not, therefore, be stated that the liberty of a person was being curtailed by an arbitrary procedure or that such a provision is violative of Article 21 of the Constitution”.

In **K.S. Anto v. Union of India** the question of double jeopardy as enshrined in Article 20 (2) in light of section 138 and section 420 of the Indian Penal Code where the court held that :

“Offences under section 138 of the Negotiable Instruments Act and section 420 of the Penal Code are different and the ingredients are different and the ingredients are also different. Convictions for different offences separately is not barred under article 20 (2). In spite of prosecutions and convictions under section 138, there will be no constitutional bar in prosecution for an offence punishable under section 420 of the Penal Code and a prosecution will be if such an offence is made out.”

Question of maintainability of criminal charge with a civil liability : There is nothing in law to prevent the criminal courts from taking cognizance of the offence, merely because on the same facts, the person concerned might also be subjected to civil liability or because civil remedy is obtainable. Civil and criminal proceedings are co extensive and not exclusive. If the elements of the offence under section 138 of the Negotiable Instruments Act are made out on the face of the complaint petition itself, enforcement of the liability through a civil court will not disentitle the aggrieved person from prosecuting the offender for the offence punishable under section 138 of the Act.

6.10. Summary Trial and Disposal (sec. 143 to 147)

1. Power of court to try cases summarily (sec143)

- (i) All offences u/s 138 to 147 shall be tried by Metropolitan Magistrate or Judicial Magistrate of first class. The Magistrate can pass a sentence of imprisonment for a term not exceeding one year and an amount of fine exceeding five thousand rupees.
- (ii) Trial should done in continuous manner on day to day basis. If adjournment is required beyond the following day, the reasons should be recorded in writing.
- (iii) Every effort should be made to conclude trial within 6 months from the date of filing.

2. Mode of service of summons (sec 144)

Summons may be serviced to the accused or witness at his usual place of residence or business by speed post or courier approved by a court of session.

3. Evidence on affidavit (sec 145)

- (i) The evidence produced by the plaintiff may be given on affidavit and may be read in evidence of any enquiry, trial or other proceeding under the Code of Criminal Procedure.



- (ii) The court may on application of the prosecution or accused, if it thinks fit, summon any person producing evidence on affidavit as to facts contained therein.

4. Bank's slip acting as prima facie evidence (sec 146)

The Court shall in respect of every proceeding under Chapter XVII, presume the fact of dishonour on basis of production of bank's slip or memo having thereon the official mark denoting that the cheque has been dishonoured, unless such fact is proved false.

5. Offences to be compoundable (sec 147)

Notwithstanding anything contained in the Code of Criminal Procedure, 1973, every offence punishable under this Act shall be punishable.

Conclusion

Though insertion of the penal provisions have helped to curtail the issue of cheque lightheartedly or in a playful manner or with a dishonest intention and the trading community now feels more secured in receiving the payment through cheques. However there being no provision for recovery of the amount covered under the dishonoured cheque, in a case where accused is convicted under section 138 and the accused has served the sentence but, unable to deposit amount of fine, the only option left with the complainant is to file civil suit. The provisions of the Act do not permit any other alternative method of realization of the amount due to the complainant on the cheque being dishonored for the reasons of "insufficient fund" in the drawer's account. The proper course to be adopted by the complainant in such a situation should be by filing a suit before the competent civil court, for realization/ recovery of the amount due to him for the reason of dishonoured cheque which the complainant is at liberty to avail of if so advised in accordance with law.

7. Discharge of a Negotiable Instrument

An instrument is said to be discharged when all rights of actions under it are completely extinguished and it ceases to be negotiable. In relation to a Negotiable Instrument, the term is used in two senses :

- (i) discharge of the instrument, and
- (ii) discharge of one or parties from liability thereon.

7.1. Different modes of discharge are as follows :

- (i) By payment in due course-This is the most obvious mode of discharge of an instrument. The payment should be made by the person primarily liable on the instrument.
- (ii) Party primarily liable on the bill becoming holder of the same.
- (iii) By express waiver by the holder.
- (iv) By cancellation of the instrument by the holder or his authorized agent.
- (v) By discharge as any other simple contract.

7.2. Discharge of a party or parties :

- (i) By payment in due course.
- (ii) Holder or his authorized agent cancelling the name of the party on instrument with a view to discharge him results in discharge of the party along other subsequent parties who have right of recourse against the party whose name is cancelled.
- (iii) If holder of a negotiable instrument releases any party to the instrument by any method other than cancellation, the said party is discharged.
- (iv) If holder of a negotiable instrument allows drawee more than 48 hours exclusive of public holidays, to consider whether or not to accept the instrument, all prior parties not consenting to such allowance are thereby discharged from the liability.
- (v) If a cheque is not presented for payment within a reasonable time and the drawer suffers loss due to failure of bank, he is discharged from liability to the extent of such damage.



- (vi) Any party, other than the party primarily liable, to whom notice of dishonour is not given by the holder is discharged from liability against the holder unless notice of dishonour is not required.
- (vii) If a holder agrees to an qualified acceptance, all prior parties who donot consent to such acceptance are discharged from the instrument.
- (viii) By operation of law-This includes discharge—
 - (a) by order of an Insolvency Court, discharging the insolvent;
 - (b) by merger of the debt under the instrument with judgement debt when a judgement is obtained against the drawer or acceptor;
 - (c) by lapse of time.
- (ix) If an instrument is materially altered, the instrument is void against the persons who were parties before the alteration if they donot consent to the alteration.
- (x) If a bill/note/ cheque is materially altered or a cheque is crossed but does not appear so on face of it and the party liable makes payment otherwise in due course, he is discharged.

7.3. Material alteration of an instrument means—

- (i) alteration which changes the character of the instrument;
- (ii) alteration which changes the rights and liabilities of the parties;
- (iii) alteration which changes the operation of the instrument.

Examples of material alterations are :

- (i) Date
- (ii) Time of payment
- (iii) Place of payment
- (iv) Sum payable
- (v) Relationship among parties
- (vi) converting an order instrument into bearer one

Examples of alterations which are not material :

- (i) Filling the blanks of the instrument
- (ii) Converting blank endorsement to 'full' endorsement
- (iii) Crossing of cheques
- (iv) Alteration made with consent of all parties
- (v) Converting bearer cheque into a cheque payable to order

8. Hundis

Hundis are indigenous negotiable instruments written in vernacular language. The term *hundi* is derived from the Sanskrit word '*hund*' which means 'to collect'. There are two main kinds of hundis :

1. Darshni hundi , i.e. hundi payable at sight
2. Muddati hundi, i.e hundi payable after a specified period.

Hundis are governed by local usage and customs. The parties may, however, exclude any prevalent custom or usage. In that case the provisions of Negotiable Instruments Act, 1881 shall apply.

9. Banker and Customer

The law regulating the relations between banker and customer are governed by –

- (i) Indian Contract Act, 1872
- (ii) The Negotiable Instruments Act, 1881.

However, these Acts are not exhaustive. The Courts refer to English Common Law whenever any point not covered by the Indian Acts arises.

**9.1. Banker**

The Banking Regulation Act, 1949 defines 'banking company' as 'a company which transacts business of banking in India,' and the term banking as 'accepting for the purpose of lending or investment, of deposits of money from public repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise.'

9.2. Customer

A person becomes a customer of a bank when the bank agrees to open an account of him. The term has not been defined by statutes.

9.3. Legal relationship between banker and the customer-special features :

- (i) A banker, having sufficient funds in the account of the customer, has legal obligation to honour the cheques of the customer. Wrongful refusal on the part of banker makes him liable to customer to claim damages.
- (ii) The banker is also under obligation to maintain proper record of transactions of customer.
- (iii) The banker has to follow the express instructions of the customer provided these are within the scope of banker-customer relationship.
- (iv) The banker may in absence of a contract to the contrary, retain as security for general balance of account, any goods and securities bailed to him by customer.
- (v) The banker has right to claim incidental charges for service provided and interest for money lent to customer as per rules and regulations.
- (vi) The banker has legal obligation to maintain secrecy about state of affairs of customer's accounts.
- (vii) The banker has right to set-off debit balance of one account with credit balance of another account of the same customer.
- (viii) The banker has right of appropriation against the customer.

9.4. A banker must dishonour a customer's cheque under following circumstances :

- (i) The customer becomes insolvent.
- (ii) The customer becomes insane.
- (iii) The customer countermands payment.
- (iv) On receiving the notice of death of a customer.
- (v) The customer gives notice of closure of account.
- (vi) The customer gives notice of assignment of credit balance of his account.
- (vii) When the banker has reason to believe that the title of the person presenting the cheque is defective.
- (viii) When the banker receives notice of loss of cheque by customer.

10. International Law relating to foreign negotiable instruments :

- (i) **Liability** – The liability of a drawer /maker is governed by the law of land where the instrument is made. The liability of the acceptor /endorser is determined by law of the place where the instrument is payable. This rule is however subject to contract between parties.
- (ii) **Dishonour** – The rules regarding dishonour are governed by the law of the place where the instrument is payable.
- (iii) If an instrument is made/drawn/accepted in a place out of India as per Indian Law, its subsequent acceptance /endorsement in India will not invalidate it even if it is invalid in a foreign country.
- (iv) The law regarding Negotiable Instrument is presumed to be same as that of India unless the contrary is proved.



QUESTION BANK - COMMERCIAL AND INDUSTRIAL LAWS

LAW OF CONTRACT, 1872

1. "Contract is void unless it fulfills the necessary conditions stated in law of contract." Discuss this statement in brief with the help of necessary elements of contract.
2. Discuss the scope of contract by evaluating the statement that – "the law of contract restricts itself to voluntarily created civil obligations".
3. "Every contract is an agreement but not all agreements are necessarily contract." Support the statement with substantial material.
4. Define offer and various modes of offer?
5. "An offer which is made by conduct is also a valid offer" Do you agree?
6. Define the communication of offer and its acceptance when completed?
7. "A notice will be regarded as sufficient only if it will convey to the minds of people in general the terms and conditions of contract." Discuss with the help of "Henderson v/s. Stevenson".
8. Define consideration. Do you agree that "Consideration must have some value in eyes of laws"? Whether contract without any consideration is a valid contract?
9.
 - (a) Define the meaning of misrepresentation.
 - (b) Contract induced by misrepresentation is a valid contract?
 - (c) Can disadvantaged party also claim damages for breach of contract?
10. "Misrepresentation and fraud carries some common point still they are distinct on some points" Discuss.
11.
 - (a) Discuss the case "Mohoribibee v/s. Dharmodas Ghose"?
 - (b) Do you agree that contract by or on behalf of minor is invalid in toto?
12. Define various modes of discharge of contract?
13. "Time is essence of contract". Substantiate with the help of ruling cases.
14.
 - (a) What do you mean by impossibility of performance of contract?
 - (b) Can agreement to do the impossible Acts is a valid agreement?
 - (c) Agreement which is initially possible but subsequently impossible did lead to valid reason for non-performance of contract?
15. Define the well established grounds for the frustration of contracts and support with the discussion of well known leading cases on it?

THE SALE OF GOODS ACT, 1930

1. Write note on "sale" and "agreement to sell"
2. Passing of risk is dependent on delivery of goods – Comment.
3. Write note on – Condition and warranties



4. Discuss the method of “Transfer of ownership and delivery of goods under the Sale of Goods Act.
5. Define Un-paid seller and his rights?
6. Discuss the duties of seller and buyer under the Sale of Goods Act?
7. Enumerate the procedure with regards to suits for breach of the contract under Sale of Goods Act?

FACTORIES ACT, 1948

1. Who is an occupier of factories under the Factories Act? When can he be exempted from liability?
2. Discuss the provisions of the Factories Act which have been enacted for the protection of health of workers?
3. A Company intends to start a factory for manufacturing machine tools and proposes to a site for the purpose. What steps the Company should take for erection of the factory premises and for occupying the same for running it?
4. State briefly the provisions of the Factories Act, which ensure safety of the workers against dangerous machinery?
5. Describe the welfare measures under the Factories Act? How are they employed?
6. What are the provisions of the Factories Act, regarding the payment of extra wages for overtime? Is it obligatory on the employees to work overtime?
7. Enumerate the provisions and restrictions under the Factories Act relating to employment of women and young persons in factory?
8. What are the provisions of the Factories Act regarding wages as provided under the Factories Act?
9. State briefly the obligation of workers under the Factories Act?
10. Explain the term manufacturing process defined under the Factories Act?
11. Describe the provisions of annual leave with wages available to a worker under the Factories Act?

INDUSTRIAL DISPUTE ACT, 1947

1. Discuss the term ‘industrial dispute’ according to Industrial Dispute Act? A sweeper employed in a firm of solicitors wants to raise an industrial dispute. Can he succeed?
2. Explain the scope of the definition of the term “Industry” in the Industrial Dispute Act. Do the Hospital run by the State Govt. and Municipal Corporation is within the definition?
3. Comment on—
 - a. Award and Settlement.
 - b. Lock out and strike.
4. What are the various authorities under the Industrial Dispute Act which help to settle industrial disputes? Discuss the function of each.
5. State the provisions of the Industrial Dispute Act with regard to the prevention & settlement of industrial disputes and voluntarily transfer of disputes to arbitration.



6. Write the provisions of the Industrial Disputes Act relating to –
 - a. Commencement of the award
 - b. Persons on whom settlements and awards are binding
 - c. Period of operation of settlement and awards
7. State the circumstances when strike and lock outs are prohibited in a public utility or otherwise? What are the effects of strikes and lock-outs in contravention of the prohibition thereof?
8. Explain what is meant by retrenchment. State when a workman can be retrenched and discuss the procedure for the retrenchment? What are the rights of retrenched worker?
9. Can the condition of service of a serviceman be changed in course of conciliation proceedings under the Industrial Dispute Act?
10. Can the workmen be punished of during the pending procedure? What procedure is to be followed by the aggrieved workman to have his grievances redressed?

WORKMEN'S COMPENSATION ACT, 1923

1. When does an employer become liable to pay compensation to workman under the Workmen's Compensation Act?
2. How far negligence or contributory negligence of the workmen's is a valid defence?
3. Discuss the defences available to an employer against a claim for compensation for personal injury made by a workman under the Workmen's Compensation Act?
4. Briefly explain the provisions relating to amount of compensation under the Workmen's Compensation Act?
5. What is the meaning of monthly wages and how are they calculated under the Workmen's Compensation Act?
6. State the provision of the Workmen's Compensation Act regarding the time for payment of compensation and penalty for default thereof?
7. Can the Compensation payable under the Workmen's Compensation Act be assigned attached or charged?
8. No claim for compensation shall be entertained by a commissioner unless notice of the accident has been given in the proper manner? Explain with reference to Workmen's Compensation Act?
9. What is the effect of the insolvency of an employer upon the right of a workman to receive compensation under the Workmen's Compensation Act?
10.
 - a. Under what circumstance a claim for compensation is entertained even though notice of accident is not given by the workmen under the Workmen's Compensation Act?
 - b. Accident alone does not entitle a workman to claim compensation; it must arise out of and in the course of employment. Comment with the help of decided cases.
 - c. Point out distinction between total disablement and partial disablement.

**THE PAYMENT OF WAGES ACT, 1936**

1. What are permissible deductions under the Payment of Wages Act and at what rate?
2. What are the duties of employer under the Payment of Wages Act?
3. "The authority under the Payment of Wages Act can investigate all claims arising out of deductions from wages or delay in payment of wages and all matters incidental to such claim" Discuss.
4. Write a note on employer's responsibility for payment of wages under the Payment of Wages Act.
5. Explain the provisions of the Payment of Wages Act relating to deductions for damage of loss?
6. When can deductions be made by an employer from the amount of bonus payable to an employee under the Payment of Wages Act?
7. State the object and scope of the Payment of Wages Act?
8. To what reasons do the provisions of the Payment of Wages Act apply?
9. What is meant by "wages" according to the Act? Would gratuity payable under settlement arrived at in course of conciliation on proceeding come within the meaning of wages? On whom does the responsibility rest for the payment of wages under the Payment of Wages Act?
10. What are the restrictions with respect to deductions from the wages for absence from duty under the Payment of Wages Act?
11. Describe the procedure for determining claims arising out of deductions for wages and state powers of the authority to whom such claims may be made under the Payment of Wages Act?

MINIMUM WAGES ACT, 1948

1. What factors are taken into account by the appropriate Govt. in fixing the minimum rates of wages of the employees of an industry to which the Minimum Wages Act is applicable?
2. Can different rate of wages be fixed for different scheduled employment under the Minimum Wages Act?
3. How can the appropriate Govt. correct clerical or arithmetical mistakes in any order, fixing minimum rates of wages?
4. Is it permissible to pay wages in kind under the Minimum Wages Act?
5. What are the remedies available to a worker who has paid less than the minimum rates of wages? State the procedure for determination of disputes under the Minimum Wages Act?
6. What are the checks against evasion of payment of minimum wages to the employee in a scheduled employment in which minimum rates of wages have been fixed by the employer?
7. Discuss the provisions of Minimum Wages Act relating to payment of –
 - (a) Wages of workers who work for less than normal working hours
 - (b) Wages of two or more classes of work
8. Define employee according to the Minimum Wages Act?
9. Elucidate the procedure for fixing minimum wages. What is the composition of such minimum rates of wages?
10. What is meant by scheduled employment under the Minimum Wages Act? Enumerate the scheduled employment? Is it a closed list?



EMPLOYEES PROVIDENT FUND AND MISCELLANEOUS PROVISIONS ACT, 1952

1. What establishment may be exempted from the operation of the Provident Fund Act?
2. State the provisions of the Employees Provident Fund Act regarding contribution to provident fund?
3. Can the employer reduce the wages of an employee?
4. Is there any priority of payment of contribution over other debts?
5. How does an individual become eligible for membership and when does his contribution begin?
6. On the death of a member, how disposal is made of his provident fund? State in your answer the arrangement for nomination of beneficiary?
7. Explain the rules governing transfer of member's accumulations in the provident fund when a member is transferred or transfers himself from one establishment to another?
8. When can provident fund be deducted from the account of members dismissed for serious and willful misconduct?
9. State the powers of appropriate government under the Employees Provident Fund Act to exempt any establishment from the scope of the scheme?
10. A decree holder wants to attach the provident fund amount standing to the credit of the judgment debtor. Advice what plea should the judgment debtor take?

PAYMENT OF BONUS ACT, 1965

1. What is the time limit on set off and set on?
2. What is the maximum amount to be set on for any given year?
3. Write a note on :
 1. Available surplus
 2. Prior charges
 3. Gross profit
 4. Net profit
4. To what establishment the Payment of Bonus Act is applicable?
5. In what two cases may bonus be payable for an establishment employing less than 20 persons?
6. What are the conditions which shall be disqualify an employee from recovering bonus under the Payment of Bonus Act?
7. State the legal provisions relating to time limit for payment of bonus?
8. What is gross profit under the Payment of Bonus Act and to what extent it differs from profit mentioned in the Balance Sheet and Profit and Loss Account?
9. If an employer does not earn profits is he liable to pay bonus? If so, describe the procedure for calculating bonus.
10. Can the unpaid and time barred bonus be recovered? How can the dispute regarding bonus be taken up by labour courts?
11. State the legal provisions relating to time limit for the Payment of Bonus Act?

**THE PAYMENT OF GRATUITY ACT, 1972**

1. What are the circumstances in which gratuity becomes payable to an employee under the Payment of Gratuity Act?
2. When does an employee fight for right of gratuity under the Payment of Gratuity Act?
3. What are the rules as to determination and recovery of the amount of gratuity under the Payment of Gratuity Act?
4. Who is the controlling authority under the under the Payment of Gratuity Act?
5. Define employee under the under the Payment of Gratuity Act?
6. Explain the procedure for claiming gratuity under the Payment of Gratuity Act?
7. Under what circumstances gratuity may be forfeited under the Payment of Gratuity Act?
8. Discuss when gratuity shall become payable to an employee? Is there any maximum or minimum amount that has to be paid as gratuity? What is the rate at which gratuity shall have to be paid?
9. Enumerate the contingencies in which the gratuity can be forfeited wholly or partially under section 4 (6) of the Payment of Gratuity Act and to what extent provisions are consistent with social justice?
10. Can gratuity payable to an employee under the Payment of Gratuity Act be attached in execution of any decree of a court?

CONSUMER PROTECTION ACT, 1986

1. Discuss the rights of consumer under the Consumer Protection Act?
2. What do you mean by consumer dispute? Who can file a complaint under the Consumer Protection Act?
3. Who is a consumer and who is not a consumer under the Consumer Protection Act? Support with leading cases.
4. What types of complaints can be taken into consideration under the Consumer Protection Act.
5. What is meaning of Service under the Consumer Protection Act?
6. Comment on "A complainant means any person in terms of Consumer Protection Act".
7. Write note on remedies available under the Consumer Protection Act.
8. Which are the Restrictive and unfair trade practice under the Act? Support with help of leading cases.
9. What is a procedure for redressal of complaints under the Consumer Protection Act? What do you mean by three tier redressal system?
10. What are the powers of national commission under the Consumer Protection Act?

LIMITED LIABILITY PARTNERSHIP ACT, 2008

1. What do you mean by limited liability partnership (LLP)?
2. Differentiate between Joint Stock Company and LLP.
3. What is the procedure of establishment of limited liability partnership?



NEGOTIABLE INSTRUMENT ACT, 1881

1. Write short on —
 - a. Bank draft
 - b. Hundi
 - c. Bill of lading
 - d. Debentures
 - e. Negotiable instruments
2. Define a promissory note. Discuss in detail essential characterizes of a promissory note with illustration.
3. What is the effect of the failure of consideration for the making of promissory note?
4. Distinguish between a promissory note and bill of exchange?
5. Write note on —
 - a. Drawer
 - b. Drawee
 - c. Drawee in case of need
 - d. Acceptance for honour
6. What is a difference between a bill of exchange and cheque?
7. When notice for dishonour is not necessary?
8. Distinction between holder and holder in due course?
9. What is meant by crossing of a cheque? What is the advantage of crossing of a cheque from the point of view of customer?
10. Explain the following terms.
 - a. Inchoate Instrument
 - b. Ambiguous Instrument
 - c. Bills of sets
11. Explain what is meant by payment in due course under the Negotiable Instrument Act?

THE RIGHT TO INFORMATION ACT (RTI), 2005

1. What is a scope and object of RTI Act?
2. Who are the Competent Authorities under the RTI Act?
3. What do you mean by Right to Information? Discuss alongwith Constitutional provisions?
4. What are the obligations of Public authorities under the RTI Act?
5. Elaborate the method for obtaining information under RTI Act.



6. Write a note on grounds for rejection to access information in certain cases?
7. Discuss the powers and functions of the Information Commission.

COMPETITION ACT, 2002

1. What is meant by prohibition of anti competitive agreement?
2. What is the procedure of preventing abuse of dominant position?
3. What do you understand by combination? Explain the procedure of regulation of Combination?
4. How is director general appointed under the Act?
5. Write short notes on :
 - a. Cartel under the Act.
 - b. Domestic Nexus
 - c. Acquisition, merger and amalgamation
 - d. Anti competitive agreement
 - e. Consumer under the Act.
 - f. Enterprise under the Act.

Section - II

AUDITING



Study Note – 5

AUDITING BASICS – I

This study note includes

- **Evolution of Auditing**
- **Definitions**
- **Major Influences of Auditing**
- **Nature of Auditing**
- **Scope of Auditing**
- **Role of Evidence in Auditing**
- **Auditing Techniques and Practices**
- **Generally Accepted Auditing Standards**
- **Concept of Materiality in Auditing**

5.1 EVOLUTION OF AUDITING

In the early days of commerce and business there was no existence of the concept of auditing. This was, may be due to the small nature of business and day to day personal control of the proprietor.

Audit can be traced back in the period 3600-3200 B.C. Initially, the audit was mainly done that of public accounts only. From historical records it appears that the ancient Egyptians, Greeks and Romans were used to the government accounts audit.

The accounts of the corporation of the city of London were audited in 12th Century. Later in Shakespeare's "Timon of Athens" the steward Flavins makes the remark "If you suspect my husbandry or falsehood, call me before the exactest auditor, and set me on the proof" which indicates the existence of an audit in the 14th century also.

In 1314, auditors were officially appointed to check the public accounts in England.

In 1494, Luca Pacioli, a French celebrated mathematician, brought the concept of Double Entry book-keeping and auditing in practice. Gradually and especially after the Industrial Revolution in the 18th century, the nature, type and size of business organizations changed. The large scale business came into existence causing dilution in the regular and direct control of the proprietor. This made it necessary to get the transactions made by the staff and representatives of owners, checked and verified by an independent person and this has given rise to concept of auditing.

In 1866, the England's Exchequer and Audit Department was created by Act of Parliament. In 1870, The Institute of Accountants in the form of a society was formed in England. It got a Royal Charter in 1880 and was turned into The Institute of Chartered Accountants in England and Wales, but before that in 1854, with a Royal Charter, The Institute of Accountants and Actuaries in Glasgow.

In India, the auditing can be traced long back in Ramayana, Mahabharata and even in the Vedas. Lord Ram asked Bharat about whether his income was more than his expenditure and vice versa. Likewise, King Yudhisthira ordered Nakula to look after the army's accounts. The system of land revenue, currency, trade and control etc. can be traced in Vedas and even in Manu Smriti. This indicates that the roots of auditing in India were rooted long back in Satya-Yuga. The sophisticated system of accounting and auditing can be found in the reign of Mauryas, Guptas and Moughals too. This first legislation relating to companies in India that is the Joint Stock Companies Act, 1857 introduced the provisions of annual audit but was made optional. Latter, The Companies Act, 1913, made it compulsory. This Act was replaced in 1956 by the Indian Companies Act, 1956, the act and the subsequent amendments not only made the audit compulsory but sought to ensure that only the independent professionals with requisites qualifications are appointed as statutory auditors of Companies. In 1965, the amendment in the Act took place and concept of Cost Audit was introduced, while the amendment in the Income Tax Act, 1961, took place in 1984 introduced the concept



of Tax Audit, Sales Tax (VAT), Trust Act, Co-operative Societies Act etc. brought the concept of different audits into practice.

A number of technological, economic changes, social events, globalization, liberalization, privatization etc. have influenced auditing to a great extent in the course of development of auditing and caused considerable changes and improvements in the techniques, principles, standards, reporting, professional ethics and responsibilities of auditor.

5.2 DEFINITIONS

The term “audit” has been derived from the Latin words “**audire**” which means to listen. In those ancient days, the person appointed to check the accounts, used to hear the explanations required from responsible officers and that’s why, the person who heard the explanations was called as an “auditor”. However, now a days, due to drastic changes in business, accounting systems, size and the provisions of different laws, this “hearing” concept of auditing is considerably changed and become more exhaustive and therefore, different authors have defined “auditing” differently, few of the important definitions are as under—

- (a) **Taylor and Perry** - “Audit is defined as an investigation of some statements of figures involving examination of certain evidence, so as to enable an auditor to make a report on the statement.
- (b) **F.R.M De Paula**- “An audit denotes the examination of Balance Sheet and Profit and Loss Account prepared by others together with the books of accounts and vouchers relating there to in such a manner that the auditor may be able to satisfy himself and honestly report that, in his opinion, such Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of affairs of the particular concern according to the information and explanations given to him and as shown by the books”.
- (c) **Prof. Montgomerly**- “Auditing is a systematic examination of the books and records of business or other organization, in order to ascertain or verify and to report upon the facts regarding its financial operations and the result thereof.
- (d) **M.L.Shandilya**- “Auditing may be defined as inspecting, comparing, checking, reviewing, vouching, ascertaining, scrutinizing, examining and verifying the books of accounts of a business concern with a view to have a correct and true idea of its financial state of affairs.
- (e) **Spicer & Pegler**- “Audit such an examination of the books of accounts and vouchers of a business, as will enable the auditor to satisfy himself that the Balance Sheet is properly drawn up, so as to give a true and fair view of the state affairs of the business, and whether the profit and loss account gives a true and fair view of the profit or loss for the financial period according to the best of his information and explanations given to him and as shown by the books, and if not, in what respect he is not satisfied”.

In the close scrutiny of the different definitions we found that there are different ways of expressing the concept auditing but having lot of similarity therein.

The meaning of an Audit contains

- (i) An intelligent and critical examination of the books of accounts of business.
- (ii) It is done by an independent qualified person.
- (iii) It is done with the help of vouchers, documents, information and explanations received from the clients.
- (iv) The auditor satisfies himself with the authenticity of the financial accounts prepared for a particular period.
- (v) The auditor reports that-
 - (a) The Balance Sheet exhibits a true and fair view of the state of affairs of the concern.
 - (b) The profit and loss account reveals the true and fair view of the profit or loss for the financial period.
 - (c) The accounts have been prepared in conformity with the concerned law.
 - (d) If he is not satisfied then reports in what respect he is not satisfied.



5.3 MAJOR INFLUENCES OF AUDITING

Now a days the techniques & process of audit ethical & professional responsibilities of an auditor, reporting method & standard, legal & statutory status of an auditor have been drastically changed compared to that of ancient days, due to the influence of different things like events, laws, revolutions etc. Some of them are—

- (a) Industrial Revolution
- (b) Ownership
- (c) Professional Management
- (d) Statutory Provisions
- (e) Case Laws
- (f) Information Technology

5.4 NATURE OF AUDITING

An audit is a dynamic concept where accountancy ends and auditing begins. An auditor has to verify the entries passed by the accountant and the final accounts prepared by him. Auditing is, therefore, the scrutiny of the accounts of business with the help of the vouchers, documents and the information given to him.

In the olden days audit was voluntary act of few businessmen having very limited scope, however the change in the form of organizations after industrial revolution had increased the scope of audit considerably.

Auditor acts according to the instructions of his client and in case of statutory audits to a certain extent regulated by the concerned law, the words “certain extent” are meant as the actual method of performing an audit is not prescribed, and never can be prescribed, and although professional auditors act on certain well defined lines can be indicated only in a general way.

A very eminent English Judge once described an auditor as a “watchdog” and not a blood hound’ which expression has been frequently quoted by others equally well informed as to the nature of an auditor’s work and of the very short period occupied by him, in the performance of his duties. An erroneous description could not be applied to an auditor, as a watchdog is a dog kept on premises for the purpose of guarding them from the damages from theft. An auditor on the other hand only appears on the scene after the damage or theft, if any, has been perpetrated, and the most he can do is to find out the amount of theft or extent of damages and also, if possible, the proprietor.

The nature of auditing is such that, the auditor will later on appear in his capacity as a critic of a book-keeper’s work, may have a great morale effect and thus prevent a cashier or book keeper from embezzling money. This morale effect has prevented theft in many more cases and is a more powerful point in favor of auditing.

5.5 SCOPE OF AUDITING

Development in the last two decades have extended the scope of auditing. Therefore, a more comprehensive definition of auditing given by Schlosser may also be considered. According to him, auditing is a “systematic examination of financial statements, records and related operation to determine adherence to generally accepted accounting principles, management policies of stated requirements”. The earlier definition of auditing by Mautz emphasizes the verification of accounting statements. While retaining that emphasis, Scholsser’s definition extends the scope of auditing by including in it an examination of allied operations. Similarly the purpose of auditing has been extended to examination of allied operations to ‘management policies or stated requirements’. This, whereas the previous definition mainly covers Mautz independent professional audit, Schlosser’s definition also covers cost audit, internal audit, Government audit, management audit, operational audit and the like.

The auditor is not supposed to perform the duties which are beyond the scope of his competence. Accounting is concerned with the recording of the transaction and preparation of statements of account but auditing involves a detailed and critical examination of accounts prepared by others. In fact, auditing begins where accounting ends.

Constraints on the scope of the audit of financial statements that impair the auditor’s ability to express an unqualified opinion on such financial statement should be set out in the report. Qualified opinion or disclaimer of opinion should be expressed as appropriate.



According to Schlosser, audit now also covers cost audit, management audit, internal audit, energy audit, excise audit, VAT audit and government audit too. Today audit is not confined to the business houses only, but also to non-business organizations. Auditor is in the nature of a watch-dog and a trustee of the nation's finances.

The scope of an audit of financial statements will be determined by the auditor having regard to the terms of the engagement, the requirements of relevant legislations. Of course the terms of engagement cannot restrict the scope of an audit in relation to matters which are prescribed by legislation or by the pronouncement of the institute. The auditor's work involves exercise of judgment for example, in deciding the extent of audit procedures and in assessing the reasonableness of the judgments and estimates made by the management in preparing the financial statements. Further more, much of the evidence available to the auditor can enable him to draw only reasonable conclusion therefrom. Because of these factors, absolute certainty in auditing is rarely attainable.

Hence, it becomes quite clear that the scope of audit is widening and there is a change in emphasis in audit objectives too.

5.6 ROLE OF EVIDENCE IN AUDITING

Meaning and Importance

The concept of evidence is fundamental to auditing. All auditing techniques and procedures are derived from it. It helps the auditor in perceiving the types of evidence available in an audit situation, collecting it through the various audit techniques and evaluating its sufficiency and competency to support accounting data. Development of this concept is therefore, basic to the understanding of the audit process. Mautz and Sharaf list the following five steps in the process of Judgment formation in auditing.

1. Recognition of the propositions to be proved.
2. Evaluation of the proposition in terms of materiality or significance.
3. Collection of evidence within given limits of time and costs.
4. Evaluation of evidence obtained as valid or not valid.
5. Formation of judgment as to the propositions at issue.

Indian Accounting Standards (AS) and their interpretations (ASI)

The auditor is required to obtain sufficient appropriate audit evidence through the performance of compliance and substantive procedures to enable him to draw reasonable conclusions therefrom on which his opinion on financial statements be based.

Types of Audit Evidence

The audit evidence influences the judgment of an auditor. The evidence need not be only documentary. Arons and Luobecke have given types of audit evidence- Physical examination, confirmation, documentation, observation, inquiries of the client, mechanical accounting, and analytical tests. While Prof. Mautz gives nine types of audit evidence – 1) physical examination by the auditor of the thing represented in the accounts. 2) Written or oral statement by independent third parties. 3) Authoritative documents- prepared inside or outside the enterprise 4) Formal or informal statement by officers and employees of the enterprise. 5) Calculations performed by the auditor. 6) Satisfactory internal control procedure. 7) Subsequent actions by the enterprise and by others. 8) Subsidiary or detailed records with no significant indications of irregularities. 9) Interrelationship within the data examined. The types of audit evidence can be grouped under the following two heads—

- (a) Analytical evidence— These evidences consist of journals, subsidiary books, allocation sheets, reconciliation statements, or any other records which supports the data appearing in the books of accounts.
- (b) Corroborative Evidence— This evidence consists of invoices, confirmations, cancelled cheques or similar documents.

Obtaining Audit Evidence:

Before obtaining audit evidence the auditor should give consideration to what types of evidence available and how to obtain them. What amount of evidence to be collected depends upon the nature and circumstances & the types of evidence to be collected depends upon the transaction and relevance of the evidence.



Auditor obtains evidence in performing compliance and substantive procedures by any one or more of the following methods-

- (a) Inspection
- (b) Observation
- (c) Inquiry and Confirmation
- (d) Computation
- (e) Analytical Review

5.7 AUDIT TECHNIQUES AND PRACTICES

Effective auditing is the outcome of systematic audit procedures applied to trade and examine audit evidence with the help of audit techniques.

According to Moyer, audit techniques are the devices or methods available to the auditor for obtaining competent evidential matter. While according to statement on audit standards, audit procedure is the act to be performed, such as reviewing, inspecting and confirming. Practice refers to the application of principles and techniques in various situations to get the expected results, on the same line auditing practice means the use of auditing principles, as were already established and notified by professional pronouncements from time to time, in different auditing situations.

Audit Techniques:

As explained above, audit techniques are the tools used to get reliable evidence while conducting an audit. According to Prof. Mautz, basically there are following ten techniques available—

- (i) Physical Examination
- (ii) Confirmation
- (iii) Comparing Documents With The Records (Vouching)
- (iv) Computation
- (v) Re-tracking Book-keeping
- (vi) Scanning
- (vii) Inquiry
- (viii) Examining Subsidiary Records
- (ix) Co-relation With The Related Information
- (x) Observation of Pertinent Activities

Professional Pronouncements

Professional pronouncements issued by professional bodies like ICAI, ICWAI, in various countries on generally accepted auditing standards regulate the auditing practice. These standards are not related only to financial and cost audit but also to other items like compilation of financial statements. Compilation with the auditing standards is a must in normal situation, and hence an auditor is expected to observe it while expressing his opinion in audit report and so he has to mention in his report whether the audit is carried out in accordance with the GAAS (Generally Accepted Auditing Standards) or not, if not the reasons thereof. As per the provisions of the Chartered Accountants Act, 1949, auditor is charged for professional misconduct if he fails to mention any material departure from the Generally Accepted Audit Procedure. **The Institute of Chartered Accountants of India** has issued number of pronouncements from time to time, which contain (i) Auditing, Review & Other Standards (formerly known as AAS) (ii) Accounting standards and accounting standards interpretation. (iii) Other statements on accounting and auditing. (iv) Guidance notes (v) Opinions (vi) Research studies/ monographs. **The Institute of Cost and Works Accountants of India** has also issued number of pronouncements from time to time, which includes- (i) Cost Accounting Record Rules and Cost Audit (Report) Rule- upto now 47 Record Rules and Report Rules have been issued. (ii) Guidance Notes- upto now about 26 such guidance notes have been issued. (iii) Research Publications- upto now 20 such research publications are issued. (iv) Research Bulletin- Bi-annual. (v) Cost Accounting Standards upto now 12 such standards have been pronounced. **The International Federation of Accountants** pronounced – (i) International Standards on Auditing. (ii) International Accounting Standards- upto now about 41 such standards have been issued. (iii) International Financial Reporting Standards.

**Accounting Standards and Accounting Standards Interpretation**

The ICAI's Accounting Standard Board has upto now issued following 32 accounting standards. These standards are based on the International Accounting Standards. These standards are mandatory and, according to Sec 227(3) of the Companies Act, the auditor is required to state whether accounting standards have been complied with or not; also in case of Tax Audit u/s 44 AB, of I. Tax Act, 1961, these standards are mandatory. The SEBI also requires the listed companies to comply with these Accounting Standards. If any company does not follow these standards, it should be disclosed in financial statements along with (i) The deviation from accounting standards. (ii) The reasons of such deviation and (iii) The financial effect, if any, arising from such deviation.

These standards are applicable to all types of organizations whether business oriented or not except activities like collecting donations and expending on earth quake relief etc. Some enterprises whose turnover in the immediately preceding financial year exceeds ` 40 lakhs but does not exceed ` 50 crores or whose borrowings include public deposits exceeds ` 1 crore but do not exceed ` 10 crores and those enterprises whose turnover does not exceed ` 40 lakhs and borrowings do not exceed ` 1 crore are exempted from the applicability of accounting standards nos. 3, 17, 18, 21, 23, 24, 25 and 27.

- AS 1- Disclosure of Accounting Policies
- AS 2- Valuation of Inventories
- AS 3- Cash Flow Statements
- AS 4- Contingencies and events occurring after the balance sheet date
- AS 5- Net profit or loss for the period, prior period items and changes in accounting policies
- AS 6- Depreciation Accounting
- AS 7- Construction Contracts
- AS 8- Accounting for research and development (withdrawn)
- AS 9- Revenue recognition
- AS 10- Accounting for fixed assets
- AS 11- The effects of changes in foreign exchange rates
- AS 12- Accounting for government grants
- AS 13- Accounting for investments
- AS 14- Accounting for amalgamations
- AS 15- Accounting for retirement benefits in the financial statements of employees
- AS 16- Borrowing costs
- AS 17- Segment reporting
- AS 18- Related party disclosures
- AS 19- Leases
- AS 20- Earning per share
- AS 21- Consolidated financial statements
- AS 22- Accounting for taxes on income
- AS 23- Accounting for investments in associates in consolidated financial statements
- AS 24- Discontinuing operations
- AS 25- Interim financial reporting
- AS 26- Intangible assets
- AS 27- Financial reporting of interest in joint venture
- AS 28- Impairment of assets
- AS 29- Provisions, contingent liabilities and contingent assets.
- AS 30- Financial Instruments : Recognition & Measurement.
- AS 31- Financial Instruments : Presentation.
- AS 32- Financial Instruments : Disclosures.



Cost Accounting Record Rules and Cost Audit Report Rules

The ICWAI had issued following 47 Cost Accounting Record Rules and Cost Audit Report Rules and these rules are mandatory as were made by the Central Government and came into force from the date of publication.

- (1) Cost Accounting Record Rules and Cost Audit Report Rules (cement) of 1997
- (2) Cost Accounting Record Rules and Cost Audit Report Rules (cycles) of 1967
- (3) Cost Accounting Record Rules and Cost Audit Report Rules (tyres and tubes) of 1967
- (4) Cost Accounting Record Rules and Cost Audit Report Rules (caustic soda) of 1967
- (5) Cost Accounting Record Rules and Cost Audit Report Rules (air conditioners) of 1967
- (6) Cost Accounting Record Rules and Cost Audit Report Rules (refrigerators) of 1967
- (7) Cost Accounting Record Rules and Cost Audit Report Rules (batteries) of 1967
- (8) Cost Accounting Record Rules and Cost Audit Report Rules (Electric lamps) of 1967
- (9) Cost Accounting Record Rules and Cost Audit Report Rules (Electric fans) of 1969
- (10) Cost Accounting Record Rules and Cost Audit Report Rules (motor vehicles) of 1997
- (11) Cost Accounting Record Rules and Cost Audit Report Rules (electric motors) of 1969
- (12) Cost Accounting Record Rules and Cost Audit Report Rules (aluminium) of 1972
- (13) Cost Accounting Record Rules and Cost Audit Report Rules (vanaspatti) of 1972
- (14) Cost Accounting Record Rules and Cost Audit Report Rules (bulk drugs) of 1974
- (15) Cost Accounting Record Rules and Cost Audit Report Rules (sugar) of 1974
- (16) Cost Accounting Record Rules and Cost Audit Report Rules (milk food) of 2001
- (17) Cost Accounting Record Rules and Cost Audit Report Rules (jute goods) of 1975
- (18) Cost Accounting Record Rules and Cost Audit Report Rules (industrial alcohol) of 1975
- (19) Cost Accounting Record Rules and Cost Audit Report Rules (paper) of 1975
- (20) Cost Accounting Record Rules and Cost Audit Report Rules (rayon) of 1976
- (21) Cost Accounting Record Rules and Cost Audit Report Rules (dyes) of 1976
- (22) Cost Accounting Record Rules and Cost Audit Report Rules (soda ash) of 1976
- (23) Cost Accounting Record Rules and Cost Audit Report Rules (polyester) of 1977
- (24) Cost Accounting Record Rules and Cost Audit Report Rules (nylon) of 1977
- (25) Cost Accounting Record Rules and Cost Audit Report Rules (textiles) of 1977
- (26) Cost Accounting Record Rules and Cost Audit Report Rules (Dry battery cell) of 1979
- (27) Cost Accounting Record Rules and Cost Audit Report Rules (sulphuric acid) of 1980
- (28) Cost Accounting Record Rules and Cost Audit Report Rules (steel tubes and pipes) of 1984
- (29) Cost Accounting Record Rules and Cost Audit Report Rules (engineering industries) of 1984
- (30) Cost Accounting Record Rules and Cost Audit Report Rules (electric cables and conductors) of 1984
- (31) Cost Accounting Record Rules and Cost Audit Report Rules (bearings) of 1985
- (32) Cost Accounting Record Rules and Cost Audit Report Rules (chemical industries) of 1987
- (33) Cost Accounting Record Rules and Cost Audit Report Rules (formulations) of 1985
- (34) Cost Accounting Record Rules and Cost Audit Report Rules (steel plant) of 1990
- (35) Cost Accounting Record Rules and Cost Audit Report Rules (insecticides) of 1993
- (36) Cost Accounting Record Rules and Cost Audit Report Rules (fertilizers) of 1993
- (37) Cost Accounting Record Rules and Cost Audit Report Rules (scraps and detergents) of 1993
- (38) Cost Accounting Record Rules and Cost Audit Report Rules (cosmetics and toiletries) of 1993
- (39) Cost Accounting Record Rules and Cost Audit Report Rules (footwear) of 1996
- (40) Cost Accounting Record Rules and Cost Audit Report Rules (shaving systems) of 1996
- (41) Cost Accounting Record Rules and Cost Audit Report Rules (industrial gases) of 1996



- (42) Cost Accounting Record Rules and Cost Audit Report Rules (mining and metallurgy) of 2001
- (43) Cost Accounting Record Rules and Cost Audit Report Rules (electronic products) of 2001
- (44) Cost Accounting Record Rules and Cost Audit Report Rules (electricity) of 2001
- (45) Cost Accounting Record Rules and Cost Audit Report Rules (plantation products) of 2002
- (46) Cost Accounting Record Rules and Cost Audit Report Rules (petroleum industries) of 2002
- (47) Cost Accounting Record Rules and Cost Audit Report Rules (telecommunications) of 2002

These cost accounting record rules are not applicable to a company though it falls under any of the above (i) if the aggregate value of the machinery and plant installed where in, as on the last date of the preceding financial year, does not exceed the limits as specified for a small scale industrial undertaking under the provisions of the Industries (Development and Regulation Act), 1951 and (ii) the aggregate value of the turnover made by the company from sale or supply of all of its products during the preceding year does not exceed ten crore rupees.

The auditor has to make mention in his report about whether the enterprise has maintained proper cost accounting records as prescribed u/s 209(1)(d).

Cost Accounting Standards (CAS)

The ICWAI had pronounced following five cost accounting standards, which the cost accountants are required to consider in order to make a standard approach towards maintenance of cost accounting record and undertaking cost audit u/s 209(1)(d) and sec.233(B) of the Companies Act, 1956. These standards equip the cost accountants with better guidelines on standard cost audit practice.

- CAS 1- Classification of costs
- CAS 2- Capacity determination
- CAS 3- Overheads
- CAS 4- Cost of production for captive consumption
- CAS 5- Determination of average (equalized) transportation cost.
- CAS 6- Material Cost
- CAS 7- Employee Cost
- CAS 8- Cost of Utilities
- CAS 9- Packing Material Cost
- CAS 10- Direct Expenses.
- CAS 11- Administrative Overland.
- CAS 12- Repairs & Maintenance Cost.

International Accounting Standards (IAS)

The International Federation of Accountants had issued the following 41 accounting standards, though these standards are not mandatory, these provide a basis for development of accounting standards in individual country.

- IAS 1- Presentation of financial statements
- IAS 2- Inventories
- IAS 3- Consolidated financial statements (superceded by IAS 27 & IAS 28 in 1989)
- IAS 4- Depreciation accounting (replaced by IAS 16, 22 & 38 in 1998)
- IAS 5- Information to be disclosed in financial statements (superceded by IAS 1 in 1997)
- IAS 6- Accounting responses to changing prices (superceded by IAS 15, which was withdrawn in 2003)
- IAS 7- Cash flow statements
- IAS 8- Accounting policies, changes in accounting estimates and errors
- IAS 9- Accounting for research and development activities (superceded by IAS 38 in 1999)
- IAS 10- Events after the balance sheet date
- IAS 11- Construction contracts



- IAS 12- Income taxes
- IAS 13- Presentation of current assets and current liabilities (superceded by IAS 1)
- IAS 14- Segment reporting
- IAS 15- Information reflecting the effects of changing prices (withdrawn in 2003)
- IAS 16- Property, plant and equipments
- IAS 17- Lease
- IAS 18- Revenue
- IAS 19- Employee Benefits
- IAS 20- Accounting for government grants and disclosure of government assistance
- IAS 21- The effects of changes in foreign exchange rates
- IAS 22- Business combinations (superceded by IFRS 3 in 2004)
- IAS 23- Borrowing cost
- IAS 24- Related party disclosure
- IAS 25- Accounting for investments (superceded by IAS 39 & 40 in 2001)
- IAS 26- Accounting and reporting of retirement benefit plans
- IAS 27- Consolidated and separated financial statements
- IAS 28- Investments in associates
- IAS 29- Financial reporting in hyper inflationary economics
- IAS 30- Disclosures in the financial statements of banks and similar financial institutions (superceded by IFRS 7 in 2007)
- IAS 31- Interest in joint ventures
- IAS 32- Financial instruments presentation disclosure provision (superceded by IFRS 7 in 2007)
- IAS 33- Earning per share
- IAS 34- Interim financial reporting
- IAS 35- Discontinuing operations (superceded by IFRS 5 in 2005)
- IAS 36- Impairment of assets
- IAS 37- Provisions, contingent liabilities and contingent assets
- IAS 38- Intangible assets
- IAS 39- Financial instruments
- IAS 40- Investment property
- IAS 41- Agriculture

International Financial Reporting Standards (IFRS)

The International Federation of Accountants had issued following International Financial Reporting Standards. Actually these standards are pronounced by the International Accounting Standard Board (IASB) constituted in place of old International Accounting Standards Committee (IASC) in 2001, this pronouncement has amended certain IAS by IFRS.

These IFRS apply to the general purpose of financial statements and other financial reporting by profit oriented entities. These IFRS apply to individual company and consolidated financial statements. The ICA of India has decided to fully converge with IFRS from the accounting period commencing on or after 1st April 2011—

- IFRS 1- First time adoption of International Financial Reporting Standard
- IFRS 2- Share based payments
- IFRS 3- Business combinations
- IFRS 4- Insurance contracts
- IFRS 5- Non current assets held for sale and discontinued operations
- IFRS 6- Exploration for and evaluation of mineral assets



IFRS 7- Financial instruments disclosures

IFRS 8- Operating segments

IFRS 9- Financial Instruments

Guidance Notes :

The ICWAI issued no. of guidance notes as for the benefit of cost accounts, which includes (i) guidance note on valuation audit under central excise law (ii) guidelines on central excise – MODVAT audit (iii) guidelines on cost audit (iv) guidelines on inventory valuation (v) total cost management in the manufacturing process (vi) guidelines on transfer pricing (vii) guidelines on CenVAT audit under central excise (viii) Environmental audit. ICAI has also issued a number of guidance notes on different auditing aspects.

5.8 GENERALLY ACCEPTED AUDITING STANDARDS PRINCIPLES (GAAS/GAAP)

GAAS/GAAP means the norms of auditing as per the provisions of law, accounting standards, auditing and assurance standard, pronouncements, guidance notes, research monographs etc. to be followed by the auditor while conducting an audit and reporting the findings. The expression was first coined by the American Institute of Certified Public Accountants (AICPA) in 1963. The generally accepted auditing standards for comprehensive audit performance approved by AICPA are really like a light house.

According to AICPA the auditor along with his training, knowledge and experience must be aware of and understand new authoritative pronouncements on accounting and auditing:

He/she should be intellectually honest, free from any obligation to be recognized as independent. He should observe the standards in field work and reporting.

(I) General Standards-

- (i) Independence- The auditor, in all matters relating to the assignments, should follow an independent attitude.
- (ii) Due Care- In exercising the work of audit, the auditor should exercise due care.

(II) Field Work Standards-

- (iii) Planning and Supervision- Before the beginning of an audit, the audit work should be properly planned and the work assigned to assistants be carefully supervised.
- (iv) Internal Control- The internal controls existing in the enterprise be studied and evaluated before hand.
- (v) Evidential Matter- While auditing, auditor should collect the evidential documents to afford a reasonable basis for forming an opinion on the financial statements.

(III) Reporting Standards-

- (vi) Financial Statements- Auditor should make a mention whether the financial statements are prepared according to the Generally Accepted Auditing Standards/Principles or not.
- (vii) Consistency- He should make a mention whether these Principles/Standards are consistently followed including current year.
- (viii) Disclosure- If auditor does not make any adverse comment in his report; the financial statements are taken as reasonably adequate.
- (ix) Obligation- Auditor should submit his report, when the work is finished, stating clearly his opinion or if not possible make a mention there in that “opinion cannot be expressed” and in such a case support it with reasons.

These formal standards/principles are framed in the context of statutory auditing but the AICPA suggest that while following these GAAP/GAAS, due consideration be given to “materiality” and “audit risk”.



The International Federation of Accountants had issued following nine broad GAAP i.e. Basic Principles governing an audit :

1. Integrity, Objective and Independence
2. Confidentiality
3. Skills and Competence
4. Work Performed by Others
5. Documentation
6. Planning
7. Audit Evidence
8. Accounting System and Internal Control
9. Audit Conclusions and Reporting

A COMPARISON – IGAAP – US GAAP – IFRS

The features of US-GAAP and Indian Accounting Standards are clear from their differences.

They are as follows :-

INDIA'S GAAP VERSUS THE US GAAP

Balance Sheet

Basis of Difference	IFRS	USGAAP	IGAAP
Format	IFRS does not prescribe any format, but stipulates minimum line items like PPE, Investment property, Intangible assets, Financial assets, Biological assets, inventory, receivables, etc.	US GAAP also does not prescribe any format, but Rule S-X of SEC stipulates for listed companies minimum line items to be disclosed either on face of Balance Sheet or Notes to Accounts.	IGAAP provides two format to Balance Sheet Horizontal and Vertical format (Part I of Schedule VI to the Companies Act, 1956).
Order	Under IFRS, line items are presented in increasing order of liquidity.	Under US GAAP, items in assets and liabilities are presented in decreasing order of liquidity.	In IGAAP, line items are presented in increasing order of liquidity.
Consolidation	Consolidation of Financial statements of subsidiaries is not compulsory until it is required under some other law or regulation	Under US GAAP consolidation of results of Subsidiaries and Variable interest entity (FIN 46R) is compulsory	It is not mandatory for companies to prepare CFS under AS 21. However, listed enterprises are mandatorily required by listing agreement of SEBI to prepare and present CFS.
Current/Non-Current	An organisation has an option to adopt Current or Non current classification of assets and liabilities	Bifurcation into current & non-current items is compulsorily required.	No such requirement


Income Statement

Basis of Difference	IFRS	USGAAP	IGAAP
Format	IFRS does not prescribe any standard format for income statement but prescribes minimum disclosure includes revenue, finance costs, share of post tax results of JV and associates using equity method.	There is no prescribed format, SEC guidelines Rule S-X prescribe minimum line items to be shown on the face of income statement & suggest 2 alternatives (a) a single step format where expenses are classified by function and (b) a Multiple step format where Cost of sales is deducted from sales	Under Indian GAAP no format is prescribed, but minimum line items have been specified in Part II of Schedule VI to Companies Act, 1956 including Aggregate Turnover, Gross Service revenue for Commission paid to Sole selling agent, Brokerage and discount on sales etc.
Prior Period Items	A prior period item/error should be corrected by retrospective effect by restatement of opening balance of assets, liabilities or equities	Mandates retrospective application of error and requires restatement of comparative opening balance with suitable footnote disclosure.	Requires separate disclosure of prior period in the current financial statement & no restatement of retained earnings are required.
Discounting	IFRS provides that where the inflow of cash is significantly deferred without interest, discounting is needed.	US GAAP also permits discounting in certain case for instance discounting is done in case of loans, debentures, bonds and upfront fees	There is no concept of discounting under IGAAP.
Change in accounting policy	IFRS requires retroactive application for the earliest period practical and adjustment of opening retained earning.	Requires prospective application of change in accounting policy and proforma disclosure of effect on income before extraordinary items on the face of income statement as separate section. Only in specific case retrospective is applicable.	Under IGAAP, effect for change in accounting policy is given with prospective effect, if the same is material.
Bifurcation of Cost	There is no specific provision in this regard.	Total cost is required to be shown separately under : (a) Cost of Sales (b) Selling and Administration (c) R & D	There is no specific provision in this regard. There are certain disclosure requirements under varied AS which should be complied.
Extra ordinary Events	Disclosure is prohibited	Nature should be both: (a) Infrequent (b) Unusual Disclosed separately on the face of Income Statement net of Taxes after results from operations	Distinct from the ordinary activities of the enterprise and, therefore, are not expected to recur frequently or regularly. The nature and the amount of each extraordinary item should be separately disclosed in the statement of P&L in a manner that its impact on current profit or loss can be perceived.



Cash Flow Statement

Basis of Difference	IFRS	USGAAP	IGAAP
Exemptions	No Exemptions	Limited exemptions for certain investment entities	Unlisted enterprises, enterprises with a turnover less than ` 500 million and those with borrowings less than ` 100 million
Direct/Indirect Method	Both allowed	Both allowed	Both allowed. Listed companies- Indirect method Insurance companies- Direct Method
Periods to be presented	2 years	3 years	2 years
Interest paid	Operating and financing activity	Operating activity (to be disclosed by way of a note)	Financing. In case of a financial enterprise, operating activities
Interest received	Operating or investing activity	Operating activity	Investing. In the case of a financial enterprise, operating activity.
Dividends paid	Operating or financing	Financing	Financing
Tax payments	Operating	Operating (to be disclosed by way of a note)	Operating
Dividends received	Operating or investing	Operating	Investing. In the case of a financial enterprise, operating activity.

5.9 CONCEPT OF MATERIALITY IN AUDITING

The concept of materiality is fundamental to the process of aggregation, classification and presentation of accounting information. It is an important and relevant consideration for an auditor who has to constantly judge whether a particular item of transaction is material or not. Obviously an auditor requires more reliable evidence in support of material items. He also has to ensure that such items are properly and distinctly disclosed in the financial statements.

According to AS 1, materiality means, the knowledge of the items disclosed in the financial statement, which might influence, the decision of the user of the financial statement. According to SA 320, "information is material if its misstatement (i.e. omission or erroneous statement) could influence the economic decision of user taken on the basis of the financial information. Materiality depends on the size and nature of the item, judged in the particular circumstances of its misstatement.

The following are some of the specific requirements in the form of Balance Sheet based materiality consideration implicit in the very process of prescribing the format in Part I of Schedule VI.

1. Loans from directors to be shown separately.
2. Nature of interest if any, of any director with the bankers or other officers of the company at any time during the year should be disclosed by way of a note.
3. The maximum due by directors or other officers of the company at any time during the year should be disclosed by way of a note.



Further whenever there is any change in the basis of accounting, the effect thereof must be disclosed.

'Audit Materiality' requires that the auditor should consider materiality and its relationship with audit risk when conducting an Audit.

Circumstances of Materiality

According to the ICAI the circumstances of materiality are as under—

- (i) Mistake discovered like valuation of stock, calculation of depreciation, calculation of interest, estimation of liability etc.
- (ii) Non-disclosure of abnormal and unusual items or non-recurring income or expenditure etc.
- (iii) Non-disclosure of items violating the statutory provisions etc.

Materiality and Audit Risk

A risk occurring due to insufficient or incompetent evidence collected by the auditor to express his opinion on the financial statement is called as an "audit risk". In case of debtors appearing on balance sheets, auditor has to express whether the figure is materially correct or not and for that he should collect the reliable confirmations from almost all debtors.

According to International Federation of Accountants, audit risk includes :

- (i) Internal Risk- Risk that material error will remain
- (ii) Control risk- Risk that client's internal control system cannot prevent or make up for such error.
- (iii) Detection risk- Risk that material errors though they are there, will not be detected.

"Audit risk" means, the risk that the auditor gives an inappropriate audit opinion when the financial statements are materially misstated. This audit risk had three components as stated above by IFA.

There is an inverse relationship between materiality and the degree of audit risk i.e. the higher the materiality level, the lower the audit risk and lower the materiality level, the higher the audit risk e.g. the risk that a particular account balance or class of transactions could be misstated by an extremely large amount might be very less, but the risk that could be misstated by an extremely small amount might be very high. The auditor takes the inverse relationship between materiality and audit risk into account when determining the nature, timing and extent of audit procedure e.g. if after planning for specific audit procedures, the auditor determines that the acceptable materiality level is lower, audit risk is increased. The auditor compensates for this by

- (i) Reducing the assessed degree of control risk, where this is possible and supporting the reduced degree by carrying out extended or additional test of control. OR
- (ii) Reducing detection risk by modifying the nature, timings and extent of planned substantive procedures.

If the aggregate of the uncorrected misstatements, that the auditor has identified, approaches the materiality level or if auditor determines that the aggregate of uncorrected statements cause the financial information to be materially misstated, he could consider requesting the management to adjust the financial information or extending his audit procedures. In any event, the management may want to adjust the financial information for known misstatements. The adjustment of financial information may involve application of appropriate accounting principles, other adjustments in amounts or the addition of appropriate disclosures of inadequately disclosed matters. If the management refuses to adjust the financial information and the results of extended audit procedures do not enable the auditor to conclude that the aggregate of uncorrected misstatements is not material, the auditor should express a qualified or adverse opinion, an appropriate.



Study Note – 6

AUDITING BASICS – II

This study note includes

- **Verification of items in the Profit & Loss Account.**
- **Verification of – Fixed Assets, Investments, Inventories, Debtors, Loans & Advances, Cash & Bank Balances, Debentures and Creditors, Provision for Taxation, Proposed Dividend & Gratuity, Contingent Liabilities, other items in the Balance Sheet.**
- **Disclosure of Accounting policies, practice, expenditure during the period of construction.**
- **Adjustments for Previous year.**
- **Provisions of the Companies Act, 1956 regarding accounts.**
- **Statistical Sampling in Auditing.**
- **Use of Ratios and Percentages for comparison and analysis trends.**
- **Inter firm and Intra firm comparison.**

6.1 VERIFICATIONS OF ITEMS IN THE PROFIT AND LOSS ACCOUNT

To verify the correctness of Profit or Loss exhibited by the Profit & Loss account, it is essential to check the items in the Profit & Loss account; these items are firstly verified from the ledger balances but this is not sufficient, the ledger balance of each item be verified from the original book of entry and the transactions regarding each item appearing on the original book of entry be checked from the original source documents. Generally, these basic documents, on the basis of which the accounting record gets created is called as Vouchers.

Voucher : By vouching we mean examination of entries in the books of prime entry with the documentary evidence. This is necessary to verify the genuineness of the document, (authenticity) legitimacy of a transaction, appropriateness, existence of approval (authorisation) and correctness of recording.

From the above definitions one can understand that, vouching means—

- (i) An examination by the auditor
- (ii) Examination of Supporting documents
- (iii) To authenticate the transactions entered in the books of Accounts

Importance of Vouching : The most important step in all types of audit is vouching of business transactions as a voucher is a foundation stone on which whole of the accounting structure stands.

The importance as well as the objects of vouching can be explained as under –

- (a) **Detection of Errors & Frauds** – Careful vouching assists the auditor to detect errors & frauds.
- (b) **Reduce liability of Auditor** – An efficient vouching reduces the auditors liability to considerable extent.
- (c) **Moral check on employees** – Detailed vouching also acts as a moral check on employees.
- (d) **Back Bone of Auditing** – Vouching done with care and caution makes an auditor to proceed well further in his work as it helps in carrying out further scrutiny with ease to satisfy him that the financial books reveal the true position of the business.
- (e) **Compliance with Law** – Auditor gets satisfied that the transactions are complying with the provisions of different laws, in particular the Companies Act.
- (f) **Capital & Revenue Expenditure** – Vouching ensures the proper allocation of expenditure into Capital and Revenue.



- (g) **Genuineness of Transactions** – Auditor ascertains that no dummy transactions are recorded.
- (h) **Nature of Transactions** – Auditor ascertains that the transactions are related to the nature of the business carried on by the client.
- (i) **Accounting period** – It enables auditor to verify the transactions related to other periods other than the period under audit.
- (j) **Accounting** – Auditor can verify whether whole accounting work is properly carried through.
- (k) **Easy conduct of Audit** – The efficient vouching creates a picture regarding organizational frame work in the mind of auditor facilitating easy conduct of audit.

Important points to be considered while vouching –

- (1) All the vouchers are serially numbered & filed in order of the entries in the accounts.
- (2) Attention should be paid to the dates which must correspond to the audit period.
- (3) The auditor should see whether the voucher is in the name of client.
- (4) He should see whether the amount written in figures and words is correct.
- (5) He should ensure whether the account head is properly written or not.
- (6) He should also see whether the voucher is signed by the recipient of the amount.
- (7) He should ensure whether the voucher is properly authenticated.
- (8) Auditor also see whether the expenditure shown is reasonable or not.
- (9) He should see whether the expenditure is for the cause of the business.
- (10) In case of expenditure exceeding ` 5,000/- auditor should ensure whether the revenue stamp is affixed on the voucher or not.
- (11) Auditor should see whether the voucher is properly accounted in the books or not.

Verification of certain items in Profit & Loss Account :**(1) Sales**

- (a) **Cash Sales** – Sales is the most important area where chances of errors & frauds are greater, hence, while verifying the cash sales, the auditor should go through the following steps—
 - (i) Initially, the auditor should carefully verify the effectiveness of existing internal check system regarding cash sales.
 - (ii) If he finds that the internal check system is efficient, he may rely thereon and may use test checking system.
 - (iii) If the internal check system is not reliable, he may resort to exhaustive verification of cash sales transactions.
 - (iv) The auditor should verify the carbon copies of cash memos and should check date, particulars of goods sold, their rates, calculation, taxes etc.,
 - (v) Check & reconcile summary of cash sales and cashier's report
 - (vi) Check whether the proper entries for Cash Sales have been passed in the cash book or not
 - (vii) Similarly, auditor may also, verify transactions in store register to ensure proper delivery of goods sold on cash basis.
- (b) **Credit Sales** – Auditor must be more careful while verifying the credit sales as documentary evidence is not as conclusive as in the case of Purchases. Following steps prove useful while verifying credit sales—
 - (i) See that the internal check system in regard to credit sales is efficient.
 - (ii) If the internal check system is efficient auditor may apply test check.
 - (iii) If the internal check system is not efficient or not in existence, the auditor should disown his liability.



- (iv) Compare the invoice with sales book to ascertain whether dates appearing on both the documents is same or not.
- (v) See that all sales invoices are recorded in the Sales book to ascertain whether payment made by the debtor is not misappropriated.
- (vi) To ensure the current recording of all credit Sales, check the order received book, goods outward register, Gate keepers register, Delivery notes, Invoices, Railway Receipts or Transport Receipts etc.,
- (vii) Check that the sale of assets is not included in the Sales book.
- (viii) Check the return inward book, to ascertain the returns, with reliable supporting documents.
- (ix) To ascertain the fictitious sales or returns, check the Sales Book of few weeks prior to the closing of the year and check the Return Inward Book for few weeks after the close of the year.
- (x) See that all credit sales from sales register are posted to respective ledger accounts.
- (xi) Check the total of sale Book & ledger accounts.
- (xii) Get the confirmation certificates / letter from the debtors and compare them with the ledger balances.
- (xiii) Cancelled invoices be checked with the duplicate copies of the invoices.
- (xiv) See that Sales Tax / VAT, insurance, transport charges are properly accounted for.
- (xv) Check the sales shown to subsidiaries, interested parties to ascertain fictitious sales with intention to inflate profit.
- (xvi) Enquire if the discount rates are different to different customers.

(2) Purchases

Auditor should examine whether the cost of purchases have been properly computed, in accordance with AS2. Special attention should be paid to related party transactions as explained in AS 18. A Management certificate be obtained regarding compliance with legal and regulatory requirements. Compare current years quantity and value, ratio of output to input etc., with that of previous year. He should examine the selected entries in the purchases book with invoice; goods receipt note and other supporting documents.

Auditor should also examine the payments after balance sheet date to ascertain unrecorded purchases. He should also, look into the following points –

- (i) Check first of all, the efficiency of internal check system.
- (ii) Verify whether purchase orders are properly authorized or not.
- (iii) Verify the purchase requisitions & quotations at random.
- (iv) Check the purchase invoices to ascertain whether they are in name of client, whether they tally with purchase orders, goods received notes, stock register and whether from the concerned supplier.
- (v) Compare the invoices with quotations to ascertain if the prices changed are according to quotations or not.
- (vi) See that all invoices are recorded in register or not.
- (vii) Check the posting from purchasers register to respective ledger accounts.
- (viii) Get confirmation letters from creditors and verify the ledger balance.
- (ix) See that purchases of capital assets are not included in purchases register.
- (x) Check the totals of purchases register & ledger accounts.
- (xi) Verify whether credit purchasers are properly exhibited in final accounts.
- (xii) Verify selected entries in purchases return book with reference to goods return note, debit note and concerned entries in creditors account.
- (xiii) Verify Bill of Lading, Customs clearance document in relation to imported goods.

(3) Wages

- (i) Auditor should satisfy himself about the efficiency of the internal check system in operation.



- (ii) Compare the current year's total wages, monthly wages, wages of each dept., ratio of wages to Sales, ratio of wages to cost of production, ratio of P.F. Contribution and E.S.I. contribution to wages etc., to that of previous year.
- (iii) Check selected entries in the wages sheet with attendance record.
- (iv) Check different deductions for I. Tax, P.F. E.S.I. etc., with the challans or returns submitted to the concerned departments.
- (v) Examine the agreement with trade union, specific awards of courts, provisions of different labour laws to ascertain their compliance.
- (vi) Examine the sanction of Casual Labour by a competent authority; check the attendance record, and also the terms of appointments.
- (vii) See that retired, expelled and resigned workers are not included in the wages sheet and for that get a list of such workers.
- (viii) See that the preparation of wages sheet and payment of wages sheet is not done by the same person.
- (ix) Disown his liability if he finds any loophole in the system of payment of wages.
- (x) Check the totals, sub totals of wages sheet.
- (xi) Check the calculations of few items here and there.
- (xii) Compare the total amount payable per wages sheet and the cheque drawn for the purpose to see that more money is not drawn than required.
- (xiii) See that the amount of unpaid wages is paid into bank immediately.
- (xiv) Compare the names of some workers, appearing in the wages sheet with the Time Cards, Job Cards, Foreman's Register and find out whether dummy workers are included in wages sheet.
- (xv) Verify whether the wages sheet is authenticated by the persons who prepared it.
- (xvi) If possible he may pay surprise visit at the time of actual disbursements of wages and see whether internal check is followed properly and whether wages are paid to the workers on presentation of their identity cards.
- (xvii) Compare the sanctioned strength of workers with the wages sheet. If the numbers of workers in wages sheet found are more, he should enquire into by verifying the respective files of personnel department.
- (xviii) Detect ghost workers appearing in wages sheet by comparing it with ESI Cards, P.F. deductions etc.
- (xix) Compare the current month's wages sheet with that of last month, if increase in number of workers found enquiry must be made.
- (xx) Signatures or attested thumb impression etc., be checked.
- (xxi) Examine the leave register to find out whether leave is sanctioned with pay or without pay.
- (xxii) To examine the genuineness of the workers signatures, compare them with Past two-three wages sheets and if required ask few workers to sign before you.
- (xxiii) See that wages are properly allocated and accounted.

(4) Salaries

Along with the above points for verifying salaries, following points should also, be considered –

- (i) Compare current years salary, ratio of salary to sales, ratio of salary to production cost, ratio of P.F. contribution to salary, with that of last years.
- (ii) Examine terms of contract and pay special attention to stock option, leave encashment, ex-gratia payment etc.,
- (iii) Check the Salary register to ascertain the actual payment of salary
- (iv) Calculate & check that deductions made from Salary are properly accounted for and paid to the appropriate authorities in time.
- (v) Verify the genuineness of the signature of employees in salary register by comparing them with previous two-three months.



- (vi) Check whether the salary of each employee gets credited directly to the employees personal bank account and if paid in cash see whether cheque drawn tallies with that of payment made to the employees.
- (vii) See whether proper accounting of the payment of salaries is done.
- (viii) Check whether increment given to employee was actually due; examine the copies of appointment letter and approval.
- (ix) Check the Return on payment of salaries and TDS therefrom submitted to Income tax department to ascertain, whether total tax deduction from employees' salary tally with the returned amount or not.

(5) Retirement Benefits

- (i) Auditor should examine that amount payable for retirement benefits like P.F., Pension, Gratuity etc., is in accordance with the provisions of the concerned laws and also the agreement with the employees.
- (ii) Auditor can use the work done by an expert in this regard i.e. can use the certificate got by the client from actuary.
- (iii) If actuarial certificate is not available he should examine the rationality of the method used in calculating the various benefits.

(6) Interest Paid

- (i) Check that amount of interest with the loan agreement.
- (ii) Compare current years ratio of interest to average loans outstanding with that of previous years.
- (iii) Verify the interest in accordance with the principles laid down in AS 16

(7) Depreciation

- (i) Verify the rates and methods of depreciation used with reference to generally accepted accounting Principles, particularly, as laid down in AS 6.
- (ii) Check the Calculations of depreciation.
- (iii) Compare current year's amount of depreciation with that of previous year.

(8) Income Tax

- (i) Check the calculations of Income Tax paid and provided and its disclosure in accordance with AS 22.
- (ii) Verify whether appropriate Provision is made for MAT, FBT etc.,
- (iii) Check the adjustments relating to assessment completed upto the audit.
- (iv) Verify whether the accounting treatment and disclosure of disputed tax liability is made with reference to the concerned accounting standards.
- (v) Check the accounting treatment relating to the Pending tax matter.
- (vi) Verify the challans of Income Tax paid.
- (vii) Check the accounting year for which Income Tax is paid.
- (viii) Verify the assessment order.
- (ix) See the interest and / or penalty for late payment of tax and filling return of Income is also accounted properly.
- (x) Check the calculations & Payments of advance tax with challans and last years liability and instruct the client accordingly.
- (xi) See whether tax audit is applicable and done accordingly.

(9) Excise Duty :

- (i) Check the Daily Stock Account to verify the excisable value and calculation of duty.
- (ii) Compare the current year's ratio of excise duty to the cost of Production with that of previous year.
- (iii) Verify the different circulars of CBE & C exempting certain goods from duty.
- (iv) Check the **CENVAT** record to ascertain whether credit taken is right or wrong.
- (v) Vouch the challans for payment of duty.



- (vi) Verify the deposits against payment of duty kept with the government and its utilization.
- (vii) Compare the Excise Returns with the actual payments made.
- (viii) Check the invoices here and there to verify the duty paid and cenvat credit availed.
- (ix) Check whether the payment of excise duty is duly authorized by the responsible person.
- (x) See that the refunds if any are taken into account while providing for Income Tax.
- (xi) See that the related items are exhibited in final accounts.
- (xii) Calculate the undisputed excise duty, but outstanding for more than 6 months and see that it is properly exhibited in the final accounts.
- (xiii) See Whether at the time of accounting the guidance note issued by the ICAI is properly followed

(10) Custom Duty

- (i) Check the payment of duty with the bill of entry, challans, clearing Agents bill etc.,
- (ii) Check whether proper accounting is done.
- (iii) See that the consumption of imported material is properly exhibited in final accounts.
- (iv) See that undisputed custom duty outstanding for more than 6 months has been properly exhibited in final accounts.
- (v) See that deduction claimed for import duty on the materials used for production of exported goods from income tax is correct and after considering the amount of refund of custom duty.

(11) Sales Tax / Vat

- (i) Compare the current years ratio of Sales tax / VAT to Sales effected with that of previous year.
- (ii) Vouch the payment of Central Sales tax and VAT with challans and return of payment.
- (iii) See whether VAT audit is applicable if so is the audit completed within prescribed time limit.
- (iv) See that the accounting of set off if any, of payment of tax is properly made and exhibited properly in final accounts.
- (v) Verify the assessment order to calculate the short or excess payment and accounting done accordingly.
- (vi) Check the assessment year in regard to payment of tax.

(12) Know How

- (i) Check the minute book to see that acquiring "Know how" is properly sanctioned.
- (ii) Auditor should see that Know How is properly accounted in the books-
 - (a) If it is related to Plant & Machinery, it should be capitalized.
 - (b) If it is regarding manufacturing process, it must be debited to P & L A/c.
 - (c) If lump sum amount is paid for both the amount be allocated between capital & revenue appropriately.
 - (d) Regular payment like royalty etc. be charged to P & L A/c.

(13) Dividend / Interest Received

- (i) Compare the current year's ratio of Dividend / Interest to the average investment with that of previous year.
- (ii) Interest received on fixed deposit be vouched with the fixed deposit receipt and the pass book. Auditor should satisfy that the Pass book presented is genuine one.
- (iii) Check the Dividend received with the Counter Foil A Dividend warrant and the covering letter and Pass book entries.
- (iv) Interest received on Securities be vouched with the securities certificates for the calculation of interests.
- (v) Ensure that the outstanding interest is properly provided in accounts.
- (vi) Check the brokers note and confirm whether the interest or dividend received subsequently in case of investments purchased or sold "Cum-Dividend" or " Ex-Dividend", Auditor should also see whether in this case proper allocation is made between capital and revenue.
- (vii) Interest received on loans granted can be vouched with the borrower's agreement.



(14) Commission Received

- (i) Compare the current year's ratio of commission received on the sales with that of previous year.
- (ii) Commission be verified with accounts of the parties from whom it is received.
- (iii) The rate of commission be verified in the agreement with the Parties.
- (iv) Amount shown in cash book be checked with the counter foil of the receipt.
- (v) Calculations of the amount of commission also be checked.

6.2 VERIFICATION OF ASSETS AND LIABILITIES

Only the vouching to ascertain the arithmetical accuracy is not enough, the auditor is supposed to go beyond that while doing audit. In all types of transactions vouching is must, but in case of capital items the auditor is required to go beyond that and verify the physical existence and evaluate the assets and liabilities to arrive at true and fair view of the state of affairs of business. Now a days it is statutory liability of the auditor to verify assets & liabilities and if he fails he is held liable for negligence. e.g. in **London Oil Storage Co. Ltd., Vs Seear Husluck and Co., (1904)**, Acct. L.R. 30-93, it was held that an auditor, who fails to verify the existence of assets as shown in the balance sheet of the company, is liable. In another case, **Arthur E. Green & Company Vs. The Controller, Advances & Discount Corporation (1920)** Act, LR xiii, it was held that an auditor is guilty of negligence, if he fails to detect time barred debts within the schedule of debts.

Verification, as defined by **Spicer and Pegler**, is "An enquiry into the Value, Ownership, Title, Existence, possession and presence of any charge on the assets", while according to **Lan Caster**, "The verification of assets is a process by which the auditor substantiates the accuracy of the right hand side of the balance sheet, and must be considered as having three distinct objects –

- (a) the verification of the existence of assets
- (b) the valuation of assets and
- (c) the authority of their acquisition.

Meaning – Verification means "**Proving the truth**". An auditor has not only to see the arithmetical accuracy and bonafides of the transactions in the books of accounts by vouching only, but has also to see that the assets as recorded in the balance sheet actually exists. The fact that there is an entry regarding purchases of an asset and has been found to be currently recorded, is not a proof that the asset is in the possession of the concern at the date of balance sheet. It is possible that after the asset had been acquired and the necessary entries made in the books of accounts, the asset might have been disposed of or pledged or mortgaged and no entry had been made regarding these facts in the books of accounts before the closing of the financial year. He has also to see whether a particular asset as appearing in the balance sheet exists or not. Verification of liabilities is also as important as the verification and assets. If the liabilities are overstated or understated, the balance sheet will not represent a true and fair view of the state of affairs of the Company.

In short, verification is a function of examining assets & liabilities to check (i) Value (2) Ownership (3) Title (4) Existence (5) Possession and (6) to see whether the assets are free from any charge or encumbrance etc.

Importance of Verification – Verification is very important function from view point of both, the auditor and the client as it gives clear idea as to true and fair view of balance sheet. The importance of verification may be described as under –

- (a) True and fair view of Balance Sheet – verification of assets and liabilities enables the auditor to comment on true and fair state of affairs of the business.
- (b) Valuation – verification enables the auditor to determine whether the assets or liabilities are overstated or under stated.
- (c) Omissions – verification facilitates the act of confirming the omission of any asset or liability in the balance sheet.

Scope of Verification – verification includes confirming of whether the assets were in existence on the date of balance sheet, whether assets had been acquired for the purpose of business only, whether the assets had been acquired under a proper authority, whether the right of ownership of the assets vested in the enterprise,



whether the assets were free from any charge and whether, the assets were properly valued and disclosed in the balance sheet.

Objects of Verification – verification of assets and liabilities is done with the following objects

- (i) To know whether the Balance-Sheet exhibits a true and fair view of the State of affairs of the business.
- (ii) To find out whether the assets were in existence
- (iii) To find out the ownership and title of the assets
- (iv) To show correct valuation of assets and liabilities
- (v) To verify the arithmetical accuracy of the books of accounts
- (vi) To ensure that the assets have been recorded properly
- (vii) To detect frauds & errors, if any
- (viii) To find out whether there is an adequate internal control regarding acquisition, utilization and disposal of assets.

Advantages of Verification – Careful verification of assets fetches the following advantages to the client –

- (a) It avoids manipulation of accounts
- (b) It guards against improper use of assets
- (c) It ensures Proper recording and valuation of assets.
- (d) It exhibits true and fair view of the state of affairs of the Company.

Technique of Verification – Auditor may adopt the following techniques for verification of assets & liabilities.

- (1) **Inspection** – This means physical inspection of the assets like counting cash in hand, measuring inventory, inspection of securities, share certificate etc.,
- (2) **Observation** – The auditor may observe or witness the inspection of assets done by others.
- (3) **Confirmation** – This means obtaining written evidence from outside parties regarding existence of assets like, confirmation from Debtors and Creditors about the balance outstanding etc.,

How to conduct the verification work

- (1) Examine the documentary evidence and see that the assets are properly recorded in the books of accounts.
- (2) Verify the opening balance from the schedule of fixed assets, ledger or register.
- (3) Verify acquisition on the basis of orders, invoices, title deeds etc.,
- (4) Verify the self constructed assets on the basis of contractors bill, work order etc.,
- (5) Ensure that the fully written off fixed assets are properly recorded.
- (6) See the authority of disposal of fixed assets.
- (7) Follow a proper procedure to ascertain the omissions, if any.
- (8) Verify ownership of the fixed assets on the basis of title deeds.
- (9) Verify existence of assets by physical verification. He should ensure that the physical verification of assets is carried out by the management.
- (10) Test check the records of fixed assets with physical verification reports and see that discrepancies, if any, are properly dealt with.
- (11) See whether the assets are charged. He should verify the Loan Agreements, Register of charge, Board Resolution, Share Holders Resolution etc.,
- (12) He should keep in mind the following points while verifying the assets & liabilities –
 - (a) Whether the assets and liabilities are properly traced from ledger to Balance Sheet
 - (b) Whether the assets are acquired for the business and liabilities got created for the purpose of business and are clearly stated in the Balance Sheet.



- (c) Whether the assets and liabilities are properly grouped under specified heads in the balance Sheet.
- (d) Whether the assets & liabilities are in actual existence on Balance Sheet date.
- (e) Whether along with ownership the possession of assets lies with the client.
- (f) Whether the assets are properly valued in the Balance Sheet
- (g) Whether the liabilities stated in the Balance Sheet tallies with the confirmation certificate.

Actual Verification of Assets & Liabilities :

(1) Plant & Machinery :

As in case of industrial concern out of total assets 20% to 50% cost is that of Plant & Machinery and hence the auditor is required to take much more precaution while verifying the Plant and Machinery and for this he should give attention to following points –

- (i) He should get the detailed list of all Plant and Machineries and asset wise accumulated depreciation.
- (ii) He should trace the opening balance in the Plant & Machinery register with the help of last year's audited balance sheet.
- (iii) He should verify quotations, invoices, cost etc., in connection with Purchase of Plant & Machinery.
- (iv) If there are sales of Plant & Machinery in audit period he should verify the invoice to that effect.
- (v) He should check the Board Resolution authorizing Purchases of Plant & Machinery.
- (vi) If any machinery is disposed off and sold as scrap during the audit period, he should check the authorization and valuers report in that connection.
- (vii) He should check the rates and calculation of depreciation and ensure these are according to the provision of Section 205 of the Companies Act, 1956.
- (viii) He should check whether related expenses incurred on purchases of machinery are duly capitalized.
- (ix) He should check whether proper accounting of profit earned or loss suffered on Sale of Machinery, during the audit period, is done.
- (x) If any machine is manufactured by the client it self, auditor should verify that capitalization of material, labor and other expenses is properly done.
- (xi) He should obtain from the Company management certificate about the verification of all items as required under CARO.
- (xii) He should scan the Plant register and physically inspect some of the major plants by visiting to the works.
- (xiii) He should, finally, ensure appropriate disclosure of all information on the balance sheet as required by the Companies Act.
- (xiv) He should obtain a certificate from the local auditor to that effect, if Plant and Machinery is kept abroad at a distant place.

(2) Freehold Land and Building :

- (i) He should see that Freehold Land and Buildings are shown separately and not mixed with lease hold or other assets.
- (ii) He should see that separate accounts for land and for buildings are mentioned because on land usually no depreciation is provided.
- (iii) He should see that the balance shown on Balance Sheet is directly traceable from respective ledger account.
- (iv) He should examine the title deeds of the property and see that the asset is in the name of the client and in the free and fair possession of the client.
- (v) He should examine that the title deed is genuine.
- (vi) The Purchases during the year be examined with the related correspondence, broker's note, auctioneer's note.



- (vii) In case of construction of the building auditor should examine the various certificates such as Builder's certificate, Contractor's certificates, Architect's certificate, Local authority certificate where needed.
- (viii) He should verify the sale, if a part of property has been sold during the period under audit.
- (ix) He should obtain a certificate from mortgagee if the property has been mortgaged and the deeds are with the mortgagee to verify the property.
- (x) Land is not subject to depreciation but see that proper depreciation is provided on building as per the provision of Sec 205 of the Companies Act, 1956.
- (xi) See that the fluctuation in the value is not to be considered on Balance Sheet but if it has been considered then see that this is properly disclosed on Balance Sheet.
- (xii) Auditor should physically verify the existence of asset.

(3) Imported Plant & Machinery :

- (i) The Auditor should examine the directors Minute Book for the resolution passed authorizing the purchases.
- (ii) The Auditor should check the RBI's permission and the import License.
- (iii) The Auditor should examine the agreement with the foreign supplier, particularly check the terms of payment, interest rates and the basis of deferred Payment.
- (iv) The Auditor should vouch the bills & receipts relating to purchases, customs duty payment, clearing & shipping charge, insurance premium etc.,
- (v) The Auditor should check the entries made in the books of accounts.

(4) Lease hold property :

- (i) He should see that the leasehold property account is separately maintained in the books.
- (ii) See that the property is in possession of client.
- (iii) Examine the lease deed to find out its value & period.
- (iv) See that the lease deed is properly registered with the Registrar. Because a lease exceeding one year is invalid unless it has been granted by a registered document.
- (v) See whether sublease is valid as per sublease agreement, in case it is granted by referring to lease agreement.
- (vi) Ascertain those conditions, the failure of which might result in the forfeiture or cancellation of lease and see whether they have been properly complied with.
- (vii) See that the lease rent and other expenses like insurance etc., regularly paid.
- (viii) In case any provision is required to be made for dilapidation (Payment on the expiry of the term of lease) see that the same is properly and continuously provided and amortized over the period of the lease.
- (ix) See that the depreciation on lease is provided by Straight line method including that of land too.
- (x) See that the written down value of lease is properly shown on Balance Sheet.
- (xi) Though lease property cannot be mortgaged, it can be sublet and if it is so, the auditor should check the agreement with the sub-lessees.

(5) Furniture & Fixtures :

- (i) Generally, furniture, fixtures and fittings are shown as one asset in the Balance Sheet, but auditor should remember that there is a distinction between them. Furniture, is movable e.g. chairs, fixture is tightly fixed to the ground e.g. science laboratory, while fittings are fitted on the walls e.g. electric wiring.
- (ii) See that furniture, fixture & fittings register is properly maintained.
- (iii) Verify that the balance from the register is correctly posted on the Balance Sheet.
- (iv) See that proper depreciation is charged in each class as per the provision of section 205 of the Companies Act, 1956.



- (v) Check the invoices, quotations, orders and authorizations in regard to new purchases of furniture during the years.
- (vi) Verify the sale of furniture and authorization for sale.
- (vii) Check whether proper accounting is done for any profit earned or loss suffered on sale.
- (viii) Physically verify the existence of the furniture, fixture & fittings.
- (ix) If acquired on lease, examine the conditions of lease and see whether these are followed duly or otherwise the lease will be forfeited.

(6) Motor Vehicles :

- (i) Ensure whether the concern is maintaining proper and separate register giving full particulars of vehicles.
- (ii) Check up whether opening balances have been properly traced in the register or not.
- (iii) Check up whether the entries regarding new purchases and sales of old vehicles have been properly recorded or not.
- (iv) Check up various documents such as agreement, invoices, bills, orders, authorizations etc., relevant to purchases & sales.
- (v) Check the auctioneer's statement, valuer's report etc., in case of sale of vehicle as scrap.
- (vi) See profit earned or loss suffered on sale is properly accounted.
- (vii) Verify whether fair depreciation on vehicles is provided or not.
- (viii) Verify registration & license to see all the vehicles are in the name of the auditee or not.
- (ix) Verify physically all the vehicles by inspecting their registration numbers.
- (x) Check the certificate from lender in case R/C book of any vehicle is lying with the lender.
- (xi) See whether proper insurance on vehicles are paid or not.

(7) Goodwill :

Goodwill is intangible but not a fictitious asset and as such has value so long it remains with the business. Therefore its value depends upon the earning capacity of the business and fluctuates accordingly. Auditor, while verifying the goodwill, will take into consideration the following points –

- (i) Auditor should see how the goodwill gets created, if there was no opening balance, verify the value from the agreement of purchasers of business, minute books etc.,
- (ii) Opening balance be verified from last year's audited Balance Sheet.
- (iii) He should check the accounts and compare goodwill account with the Balance Sheet to ensure that goodwill account is clearly stated in the Balance Sheet and no other asset is mixed with it.
- (iv) Satisfy himself by making a reference to the Articles of Association or Partnership Deed, as the case may be, if value of goodwill is enhanced or reduced during the year under audit.
- (v) Since goodwill is an intangible asset, verification of charge on it doesn't arise.
- (vi) As goodwill is always valued at cost, a question of providing depreciation on it doesn't arise.

(8) Investments :

- (i) Insist on a schedule of investments, when number of investments held by the auditee is very large.
- (ii) Examine the investment schedule with reference to the relevant ledger accounts.
- (iii) See that the investments have been shown properly in the Balance Sheet
- (iv) He should verify the existence of investments by inspecting the certificate, deposit receipts etc.,
- (v) Obtain a certificate from bank of certain securities given to the bank for safe custody.
- (vi) Examine the transfer deed, broker's contract note if certificate of investments is not received upto the date of audit of the securities purchased during the year under audit.
- (vii) Examine the trust deed if securities are held by a trust on behalf of the client.



- (viii) Verify the Sales proceeds from pass book of the sale of any securities made after the date of Balance Sheet but before the audit.
- (ix) Verify relevant vouchers and certificates whether securities are free from any charge or not
- (x) See whether investments are properly valued or not giving consideration to the provisions of the Articles of Association in case of trust companies as they are valued at cost but in case of finance companies they are valued, being traded as current assets, at cost price or market price, whichever is less.
- (xi) See that regarding the investments in subsidiaries, disclosure requirements of section 212 are complied with.
- (xii) Check the balance in the schedule of investments in the name of the client and compare it with the general ledger and Balance Sheet. See that the investments are in the name of the client.
- (xiii) See that investments made by the company are not contrary to the provisions of section 372 of the Indian Companies Act, 1956.
- (xvi) In case of application money paid for shares which are still to be allotted, the fact is to be specifically disclosed in Balance Sheet.
- (xvii) Confirm that uncalled amount on partly paid shares held as investment is shown as contingent liability in Balance sheet.
- (xviii) The auditor has to report, as per section 227 of the Companies Act, whether any shares, debenture sold at price lower than their cost, in the case of finance company, whether proper records of investments are kept.
- (xix) While auditing the investments the auditor should keep in mind the provisions of AS 13.

(9) Patents, Trade Marks and Copy Rights :

(A) Patents

- (i) Examine the patents and verify them with the help of the certificate from the party granting the patents.
- (ii) Ensure that the patents are duly registered in the name of the auditor.
- (iii) Verify the voucher, pass book, agreement, authorization etc., in case of outright purchases of patents and see that the cost is fully capitalized.
- (iv) Check the renewal fees, if any, paid is debited to Profit and Loss Account.
- (v) In case of patents developed by the client, expenditure incurred on its development, should be capitalized.
- (vi) Call for schedule in case the number of patents is large and examine the dates and acquisition, description and expiry date etc.,
- (vii) Question of charge on patents does not arise as it itself is a right in use.
- (viii) See that proper depreciation is provided on patents as per the provision of the Companies Act.

(B) Trade Marks

- (i) See that the trade marks are registered in the name of the auditee.
- (ii) See whether it is shown distinctively in the Balance Sheet.
- (iii) Check the Assignment Deed to ascertain the Terms and Conditions of the acquisition of Trade Marks to see whether the terms are followed properly.
- (iv) Obtain a schedule of Trade Marks if those are in large numbers.
- (v) See that the renewal fee is regularly paid.
- (vi) Verify the valuation of Trade Marks to see whether it is properly done or not.

(C) Copy Rights

- (i) Verify copyrights with agreements.
- (ii) See whether revaluation of copyrights is made properly and profit or loss is properly accounted.



- (iii) Obtain the certificate of approved valuer to that effect.
- (iv) See that the balance exhibited on balance sheet can be traced from ledger account.
- (v) Verify the opening balance from last year's audited balance sheet.

(10) Sundry Debtors

- (i) Trace the opening balance from last year's audited Balance Sheet.
- (ii) Obtain Sundry Debtors' schedule from the management and compare it with ledger accounts.
- (iii) See the debtors are shown properly on Balance Sheet.
- (iv) See that the provision for bad debts, discounts etc., is properly made.
- (v) Examine the relevant vouchers, minute book for verifying whether bad debts written off are correct or not.
- (vi) See that the legal requirements of schedule of the Companies Act, 1956 are duly complied with. For this purpose the debtors are to be classified as –
 - (a) Debtors outstanding for a period exceeding six months and
 - (b) Other Debtors also, particulars to be given separately of –
 - (c) Debts considered good and in respect of which the Company is fully secured.
 - (d) Debts considered good for which the Company holds no security other than the debtors' personal security.
 - (e) Debts considered doubtful or bad. Over and above these requirements, Debts due by directors or other officers of the Company or any of them either severally or jointly with any other person or debts due by firms or Private Companies respectively in which any director is a partner or a director or a member to be disclosed separately. Debts due from other Companies under the same management to be disclosed with the name of the Companies. The maximum amount due by directors or other officers of the Company at any time during the year to be shown by way of a note.
- (vii) If the customers have purchased the goods on hire purchase basis and some of the installments are not due, the same is not to be shown as debtors, instead they are to be shown on "Stock out on "hire purchase" at cost.
- (viii) If the goods are sold on Sale or approval basis, such customers cannot be shown as debtors unless they have agreed to purchase the same before the date of the Balance Sheet.
- (ix) Whenever there are credit balance in debtors accounts, the same should not be deducted from other debtors' debit balance. Such credit balance is to be shown on the liability side separately.
- (x) Enquire whether there is any dispute regarding any balance included in debtors. The auditor should verify the document regarding any dispute.
- (xi) The auditor should ascertain that there are no unrecorded debtors and for he has to examine the cut off transactions. He should examine the cut off procedures to ensure separation of transactions of the current year from the next year. Sale of the current year should be separated from the sale of next year. He shall ensure that sales bills are prepared for goods dispatched. No sales bills are raised unless the goods are actually dispatched and sold during the accounting year.
- (xii) The auditor shall check collection from debtors in the next year to decide whether the year end balances are good or not. If debtor has become insolvent, after the date of Balance Sheet, such debtors should be provided for.
- (xiii) The auditor should arrange to send the letters of confirmation balance by the client as per clients record and see that the reply of confirmation is forwarded to his office directly, usually this should be sent within 15 or 20 days of year ending date under the supervision of audit staff. After the reply is received, the same should be tallied with the balance shown in the debtors ledger and differences, if any, be reconciled.

**(11) Stock in Trade**

This is an important asset and may be used to fabricate profit and give misleading Balance Sheet and hence an auditor is required to take lot of care and caution while verifying stock in trade and for following points be considered –

- (i) Verify whether an efficient internal check system regarding stock is in operation or not.
- (ii) Compare the stock register with purchases and sales book, in regard to question
- (iii) Check the gate keepers' outward register to find out whether any fictitious sales has been entered in Sales Book.
- (iv) Check the Stock sheets and Calculations, additions, costing etc., there in.
- (v) See that goods sold but not delivered are not included in Closing Stock.
- (vi) See that goods purchased, invoices received but delivery yet to be received are included in the Closing Stock.
- (vii) See that goods received from others to be sold on their behalf are not included in Closing Stock.
- (viii) See that furniture, tools etc., are not included in Closing Stock.
- (ix) Compare the balances of Stock Register with the Stock sheets.
- (x) Method of stock taking may be enquired into, to find out possibilities of frauds and errors.
- (xi) Examine the principle followed in the valuation of stock to ensure that those were followed in previous years.
- (xii) Check whether stocks are valued on the basis of "Cost price" or "Market price" whichever is less or not.
- (xiii) Compare the Gross Profit rate of current year with that of previous years, if considerable variation is found, that should be enquired into in detail.
- (xiv) Determine the obsolete, slow moving, non-moving and damaged item and ascertain their treatment in accounts.
- (xv) Obtain a certificate from the management to the effect that the stock sheets are accurate and confirming that they have been signed by responsible person.
- (xvi) In case of the manufacturing concern the goods may be of following categories and should be valued and verified after taking above points into considerations and checking the relevant cost recorded like purchases requisitions, material requisitions, goods received notes, bin card and stores ledger etc.,
 - a] Raw materials b] Work in Progress c] Finished goods d] Stores & Spare parts.
- (xvii) Ensure that the various components of Stock have been separately disclosed in the Balance Sheet with their mode of valuation.

(12) Loose Tools

Loose tools at the end of the year should be checked by the auditor as follows :

- (i) The auditor should see that the cost of loose tools is properly determined and certified by the Chief Engineer.
- (ii) If the loose tools are manufactured by the organization, the authorized officer shall certify the value of such tools.
- (iii) He should physically verify these tools or obtain a list of tools duly certified by the responsible officer. Any discrepancies shall be investigated.
- (iv) Ensure that the closing stock of tools is valued at cost. See that the valuation is done on the basis, which is consistent taking in to consideration obsolescence, damage, brokerage etc.,
- (v) See that the loose tools are disclosed in the Balance Sheet on asset side under the head "Current Assets".



(13) Live Stock

- (i) See the live Stock Register and note down carefully the particulars like breed, year of purchases, purchase price, depreciation etc., for various categories of animals.
- (ii) See that some identification number is given to identify the animals.
- (iii) Examine the basic of valuation of animals. In case the animals are purchased at the age of maturity the cost will include Purchase Price plus freight. If the animal is reared from its conception and then brought to Maturity the cost includes cost of calving, cost of fodder etc., consumed till maturity and the suitable share of overheads.
- (iv) See that the cost up to the maturity stage of animal has been written off once the earning capacity of the animals starts declining over the remaining life.
- (v) Ensure that disposal value at the end of the life of the assets has been adjusted properly.

(14) Bills Receivables

- (i) Get the schedule of bills receivables from the management.
- (ii) Check the total of the Schedule with the ledger.
- (iii) Check each bill to ascertain whether it is properly drawn, signed by the drawee and properly stamped or not.
- (iv) Verify the Cash received on the matured bills after Balance Sheet date.
- (v) Check the bills discounted with the B.R. Book and Cash Book.
- (vi) See that relevant foot note by way of contingent liabilities regarding bills discounted but yet not matured, properly appears on Balance Sheet.
- (vii) Verify the bills deposited with bank for safe custody or for collection or for securities of loans, with the bank certificate to that effect.
- (viii) Check the cash book and rebate / discount in connection with the proceeds received from retired bills before maturity.
- (ix) Trace the balance shown in Balance Sheet from the ledger account.
- (ix) Check the opening balance from last year's audited Balance Sheet.

(15) Cash at Bank

- (i) Compare the balance as shown in the Pass Book with balance of Cash shown in the bank column of Cash Book.
- (ii) Prepare Bank Reconciliation Statement to ascertain the reasons behind the difference between Pass book balance and Cash book balance.
- (iii) Obtain a balance certificate from the bank in case of suspicion of presentation of fictitious pass book and compare the balance with Cash book.
- (iv) Obtain separate certificates for different accounts or deposits with the bank for proper verification of different balances.
- (v) See that "The charges not yet collected" are genuine and not made up in order to conceal the deficiency.

(16) Cash in Hand

- (i) Visit the auditee's premises and physically count, whole of the cash at a time and compare it with the balance shown on Cash Book.
- (ii) He should not accept IOU's as cash.
- (iii) If cash could not be counted on last day of the year he may visit as per his convenience and count the cash and check the cash book from the end of the last year to the date as and when cash is counted to verify the correctness of each balance at the end of last year.
- (iv) If actual cash counting is not possible ask the auditee to deposit whole of the cash in hand at the close of the year into bank, then the Closing Cash Balance gets automatically checked.



- (v) Whatever it may be, auditor should pay surprise visit to auditee and count the cash to prevent the cashier to borrow money and make up the deficiency which was due to embezzlement in the past.
- (vi) Get certificates from the auditors of the branches about the cash balance in hand and their correctness.
- (vii) Check the documentary evidences in reference to the cash in transit.
- (viii) See that the cash in hand is properly shown on the Balance Sheet.

(17) Petty Cash

- (i) Count the cash physically on the closing date of the year and compare it with the balance shown on Petty Cash Book.
- (ii) If not possible, visit on any day and count the cash balance at the time of balance on main Cash Book simultaneously and check the accounts from the year end to the date of counting.
- (iii) See whether it is shown properly on Balance Sheet including Cash in hand.

(18) Loans and Advances

Loans and advances may be of different types like –

- (a) Loans against the security of Land & Building.
- (b) Loans against the security of goods.
- (c) Loans against the security of stocks & shares
- (d) Loans against the security of Insurance Policies
- (e) Loans against the personal Security of the borrower.

Therefore, in each case the duty of auditor in general is as under:

- (i) Examine whether a proper loan ledger has been maintained upto date or not.
- (ii) Examination of the Security ledger against each loan.
- (iii) Examine the loan agreement and find out the rate of interest, due dates of installments, penalty, interest etc.,
- (iv) Ascertain whether any loan is doubtful of recovery. In case it is doubtful, a provision for the expected loss is to be made.
- (v) Verify that loans have got proper sanction from the authority.
- (vi) Obtain a letter of confirmation from the parties to whom loans are advanced.
- (vii) In case of loans to directors, prior approval of the Central Govt. is obtained.

(A) Loans Against The Security of Land & Buildings

- (i) Examine the mortgage deed in depth and to confirm that the mortgage has been properly executed in favour of the lender.
- (ii) Examine the title deeds deposited.
- (iii) Examine the Valuer's certificate, in order to verify the value and see that the value is adequate.
- (iv) Confirm that the property is properly insured and insurance premium has been paid in time.
- (v) Examine the title of the borrower in connection with property etc.,
- (vi) Take the acknowledgement of title deeds from the first mortgage in the case of second mortgage.
- (vii) Confirm that the mortgage is properly registered.
- (viii) The amount of loan should not be more than two thirds of the value of property.
- (ix) The auditor should enquire the rated interest and the date on which it is payable; if the loan has been outstanding for a long time, he should make an enquiry when the interest has not been paid.
- (x) In the case of loan on mortgage of lease hold land, the auditor should see that the ground rent has been paid regularly by the borrower on the due date.
- (xi) In the case of part repayment of loan, the auditor should get the loan confirmed.



(B) Loans Against The Security of Goods

- (i) Examine the nature of the goods and confirm that the goods are belonging to the borrower.
- (ii) Verify whether loan is granted against railway receipts, lorry receipt, dock warrant, godown keeper's receipt etc.,
- (iii) See that the rent of godown is paid in full and the goods are fully insured if the goods are stored in godown.
- (iv) Examine the value of goods by comparing them to the present market value. He may rely on the inspector's report regarding quantity and quality.
- (v) Examine the turn over of the client if the goods are perishable.

(C) Loans Against Security of Stocks & Shares

- (i) Call for a statement of stocks and shares given as security.
- (ii) Confirm that all shares are fully paid up
- (iii) See that an instrument of transfer, properly stamped is available for his checking.
- (iv) See that the value is properly disclosed as per the market rates.
- (v) Ensure that there is a sufficient margin for the loans advanced.
- (vi) Ensure that the charge is properly registered.

(D) Loans Against The Security of Insurance Policies

- (i) See that the policy has completed at least two years from the date of the first premium.
- (ii) Confirm that all the premiums have been properly paid and policy is in force.
- (iii) Ascertain that the due notice has been given to the insurance company.
- (iv) See that loan has been advanced on the basis of surrender value of the policy as certified by the insurance company.
- (v) Confirm that the premium, if any, paid by the lender to keep the policy in force is debited to loan account of the borrower.

(E) Loans Against Personal Security of The Borrower

Examine the documents like promissory note, guarantor's details and income certificate of the borrower.

(19) Trade Creditors

- (i) Ask for a schedule of creditors and check the same with purchase ledger already examined by him.
- (ii) Verify posting in the purchase ledger
- (iii) Ensure that all purchases made during the year especially at the end of the year are included in the accounts of the creditors.
- (iv) In case of suspicion, ask for the statement of account to be sent and verify the same along with scrutiny of ledger account and reconcile the differences, if any,
- (v) See the various debits given for discount, goods return etc., are genuine
- (vi) Enquire into the reason for non payment of overdue creditors. It is possible that amount might have been misappropriated.
- (vii) Examine some purchase invoices and confirm that they are relating to the year under audit.
- (viii) Test check returns and see that they are supported by credit notes of the suppliers.
- (ix) Obtain confirmation from the parties.

Also, the auditor should keep in mind the following guidelines about audit of creditors.

(I) Internal control – The auditor should review the following aspects of internal control relating to creditors –

- (A) Proper recording of transactions and linking of payment with outstanding.
- (B) Periodical schedule of creditors.



- (C) Follow up action on overdue accounts
- (D) Payment to creditors as per the approved policies.
- (E) Statement of accounts obtained from creditors.
- (F) Proper adjustments in creditors accounts regarding purchase returns, cash discount, trade discount etc.,
- (G) Cut off Procedure regarding creditors.

(II) Verification – The auditor should employ the following procedures

Examination of Records –

- (A) Carryout appropriate procedure to judge the adequacy of cut off procedure. Ensure that documents relating to receipt of goods before the year end are recorded.
- (B) Look into the difference between total of creditors balance and the control account balance
- (C) Examine relevant correspondence for verification of validity, accuracy and completeness of creditors.
- (D) Pay attention to outstanding items claims for short supply, poor quality, discount etc.,
- (E) Examine correctness of transfer from one account to another.
- (F) Examine any unusual payments at the end of the year.
- (G) Confirm material liabilities at the end of the year.

Confirmation

The direct confirmation for creditors is similar to that adopted for debtors.

Disclosure

The auditor should examine whether creditors are disclosed properly in the financial statements.

Certificate from the Management

Obtain a certificate from the management that all the known liabilities have been recorded in the books of accounts.

Working Papers

The auditor should verify all the working papers relating to creditor.

(20) Debenture

- (i) Examine the provisions regarding the powers of the company to issue debentures as contained in Memorandum and Articles of Association.
- (ii) Examine the terms of debenture issue as contained in Trust Deed and ensure that the same have been properly complied with.
- (iii) Verify cash received on this account with the help of Cash Book entries.
- (iv) Verify whether the interest on debentures is paid properly at regular intervals.
- (v) Confirm redemption of debentures on the basis of minutes of Board of Directors, counter foils of the cheque books, Bank Pass Book and Cash Book, returned debentures certificates etc.,
- (vi) Issue of debentures as a collateral security should be disclosed in the Balance Sheet.
- (vii) Confirm whether the debentures are secured or unsecured and see that the same is disclosed properly.
- (viii) The auditor should see that there is a proper board resolution passed regarding issue of debentures.
- (ix) The auditor should check the limit on borrowings including debentures as per section 293. In case the limit is likely to be crossed, the share holders in the annual general meeting can pass an ordinary resolution to increase the limit.
- (x) The auditor should see that necessary permission of the SEBI has been obtained by the company before issue of debentures.
- (xi) The auditor has to see that in case debentures are offered privately, the statement in lieu of prospectus is filed with the Registrar of Companies. In case of public offer the prospectus is issued.



- (xii) The auditor should verify the charge and its registration with the Registrar of Companies. 49
- (xiii) See that a Sinking Fund has been created if it is and the terms of issue of debentures and the transfer from Profit & Loss account is under each year as per following SEBI guide lines –
 - (A) Fully convertible debenture having conversion period more than 36 months is not permissible unless conversion is made optional.
 - (B) In case of Non-convertible debentures or partly convertible debentures credit rating from credit rating agencies is to be obtained before issue, if the maturity period exceeds 18 months.
 - (C) In case of issue of debentures with maturity period above 18 months appointment of debenture trustee or creditor of Debenture Redemption Reserve each year is a must.
 - (D) Period of maturity, redemption amount, yield on redemption shall be indicated in the prospectus.
 - (E) Premium amount at the time of conversion for PCD shall be determined and stated in the prospectus.
 - (F) While raising money by way of debentures the present and projected debentures equity ratio, servicing behavior of existing debentures, payment of interest on due dates on term loans and debentures, certificate from financial institution about their no objection for a second charge are to be disclosed.
 - (G) Debenture Redemption Reserve should be created either in equal installment for the remaining period of debenture life or at a higher amount of profits permit.
 - (H) In case of PCDs, the DRR should be created for a sum equivalent to non-convertible portion of debentures.
 - (I) The trustees to the debenture holders will supervise implementation of the conditions regarding creation of security for debentures and regarding the debenture redemption reserve.

(21) Provision for Taxation

- (i) See that the provision for taxation made in the current year is adequate taking into account the profit made, deductions and any other allowances as per Income Tax Act. The auditor should see that suitable adjustment is made in respect of additional demand or refund as the case may be. Material Tax liability for which no provision is made should be disclosed in the report.
- (ii) Get a Statement of Income.
- (iii) Vouch advance payment of Income tax referring to the challans and bank statements.
- (iv) Ensure that Provision for taxation for the current year is shown separately in the Profit and Loss account and in the Balance Sheet.
- (v) In case the tax liability determined is more than that provided for against which the company might prefer an appeal before the high authority, a reference to this effect should be made in the accounts. Where an application for rectification of mistakes u/s 154 of the Income tax Act, has been made the amount of tax decided is considered or disputed. As per AS4, the disputed tax liability may require a provision and suitable disclosure. The auditor should enquire from the management, review minute of the meeting of the BOD and correspondence with the lawyers for determination of the Provisions.
- (vi) Examine the assessment completed, revised or rectified during the year.

(22) Provision for Proposed Dividend

- (i) See that there is an adequate Profit for declaration of dividend.
- (ii) Check the minute books recommending dividend to ascertain the rate of dividend recommended.
- (iii) Verify the calculation of proposed dividend and see whether it is provided on the paid up share capital only, excluding the calls in arrears and forfeited shares.
- (iv) See that it is properly exhibited in the final accounts.

**(23) Provision for Expenses Not Allowable Under Income Tax Act**

- (i) The expenses not deductible in the calculation of tax liability can be debited to profit and Loss account, hence auditor should verify if any of such expenses appear in Profit and Loss accounts.
- (ii) Verify the correctness of the amount.
- (iii) See whether those 'not allowable expenses' are re-added in the profit of the year to calculate the expected tax liability and the provision for taxation is made accordingly or not.

(24) Secret Reserve:

Any reserve not appearing on the Balance Sheet is called as a Secret Reserve. The existence of the reserve may be inferred from an intelligent verification of the accounts by the auditor even though the amount cannot be ascertained. Generally such type of reserve appears in financial institutions and insurance companies. Secret reserve may be created by –

- (i) Writing down the assets much below their cost
- (ii) Providing excessive depreciation
- (iii) Providing more reserve for doubtful debts etc.,
- (iv) Writing down the goodwill considerably
- (v) Omitting certain assets from Balance Sheet
- (vi) Charging capital expenditure to revenue account
- (vii) Over valuing the liability.
- (viii) Showing contingent liabilities as real liabilities etc., According to the Provisions of Companies Act, 1956, creation of Secret Reserve is prohibited except in the case of banking, financial, insurance and electricity companies.

To verify the secret reserve, if any, the auditor should keep in mind the following points :

- (i) Carefully enquire into the necessity of creating such reserve.
- (ii) Don't qualify audit report if it is found that the intention of the company is honest and the amount is reasonable.
- (iii) May pass a remark in audit report that the assets are understated,
- (iv) Discuss the fact, if found, that the director's intention behind creating secret reserve was not honest and only to facilitate improper dealing in shares.

(25) Contingent Liabilities :

The liability which depends on happening or not happening some thing is called as contingent liability. This liability may involve payment of revenue nature incurring losses or involves the acquisition of asset.

Examples –(i) Disputed claims by workers for compensation

- (ii) Bills Discounted
- (iii) Guarantees given in favour of others
- (iv) Amount on incomplete contracts
- (v) Calls unpaid on partly paid shares
- (vi) Payment of gratuity under Industrial Dispute Act,
- (vii) Preference dividend in arrears.

Verification –

Auditor should carefully verify contingent liabilities as it may become actual liability on happening or not happening certain events and while verifying keep in mind following points.

- (i) Obtain certificate about the contingent liabilities disclosed in the Balance Sheet, from a responsible officer.
- (ii) Carefully examine whether such liabilities are in existence or not.



- (iii) Check relevant documents to confirm the existence of contingent liability.
- (iv) Verify the certified list given by responsible officer to ascertain whether there exists any contingent liability which may turn to be an actual liability.
- (v) Verify whether proper provision is made or not for the contingent liability turned out to be an actual liability.
- (vi) Verify bill discounting register, investment register, minute book and other relevant records to establish the amount of contingent liability.
- (vii) See whether contingent liability is properly disclosed in the Balance Sheet.

(26) Capital Reserve :

It is not defined by the Companies Act, 1956. It may be defined as any profit or reserve earned on sale or purchase of capital asset and / or business and which cannot legally be distributed among share holders. It is created out of abnormal and non-trading profits like premium received on issue of shares, balance remaining after reissues of forfeited shares on share forfeited account, profit earned on amalgamation, absorption or reconstruction of companies, Capital Redemption reserve, Profit prior to incorporation etc. While verifying this reserve an auditor should keep in mind, following points –

- (i) See whether the capital profits transferred to this reserve are really surpluses of capital nature or not.
- (ii) See whether the Capital Reserve is utilized according to the provisions of Articles of Association or not.
- (iii) See whether it is properly exhibited on Balance Sheet or not.

(27) Gratuity:

- (i) Auditor should see that proper provision is made for the gratuity and if not whether the auditee has disclosed the amount not provided for
- (ii) As provided in the Companies Act, amended in 1988, the auditor should qualify his report if the company has not provided for gratuity either wholly or partly.
- (iii) He should check the calculation made for provision of gratuity and confirm whether it is based on the periodical actuarial valuation or not.
- (iv) See whether gratuity is provided for on a net of tax basis then the gross amount is properly disclosed.
- (v) See that the method used for calculating the provision for gratuity is disclosed and see the significance of such cost to the company.
- (vi) Auditor should keep in mind the provisions of AS 15 while verifying the provision made for gratuity.

(28) Valuation of Assets –

Along with vouching and verification of assets and liabilities, valuation is an important task auditor has to perform, without which verification of assets cannot be said as complete and the Balance Sheet cannot be taken as showing true and fair view of the state of affairs of business.

Valuation, here, does not mean actual calculation and determination of the value of each and every asset by the auditor but it implies the testing and checking of the values of assets shown in Balance Sheet, which also, included to see whether values of assets are based on generally accepted accounting principles.

Valuation Procedure –

For Valuing the different assets, shown on Balance Sheet; the auditor has to follow following steps –

- (i) Obtain the schedule of valuation prepared by the management
- (ii) Examine and critically analyze all figures
- (iii) Get information about the valuation process adopted by the auditee
- (iv) Test the values of different assets given by management at random



- (v) Ensure whether the valuation is done on the basis of Generally Accepted Accounting Principles e.g. fixed assets at value of cost less depreciation, current assets at cost or market price whichever is less etc.,
- (vi) Verify if the valuation process adopted by the auditee is followed from year to year.
- (vii) Enquire about variation, if any, in the process of valuation.
- (viii) Take, if necessary, assistance of technical persons, approved valuer's for the purpose of ascertaining the current values of assets.
- (ix) Verify the accuracy of depreciation provided, capitalization of revenue expenditure etc.,
- (x) See that proper value of assets be exhibited on Balance Sheet.

6.3 DISCLOSURE OF ACCOUNTING POLICIES AND PRACTICES

Under the Indian Companies Act, 1913 the annual accounts were required to exhibit a “true and correct” view of the State of Affairs of a company. According to the Companies Act, 1956 however the annual accounts are required to disclose a “true and fair” view of the state of

affairs of the company. The changes from “Correct” to “Fair” is very significant.

The Indian Companies Act 1913 laid emphasis on mere reproduction and required preparation of annual accounts strictly in accordance with the books of accounts. The Companies Act, 1956 has however used the term “Fair” in a completely different sense. The word denotes a representation on the state of affairs of the company. Thus the emphasis has been shifted from arithmetical accuracy and reproduction, to the presentation of annual accounts in such a manner as to disclose a fair view on the Balance Sheet concerned, of the state of affairs of the Company on the date of the Balance Sheet and in case of the Profit and loss account, of the profit or loss for the financial year concerned.

This shift has brought on the shoulder of the auditor much more responsibility from what he had previously. The auditor must be careful to see that the accounts show a fair picture to the share holders and others concerned. To achieve this objective, the auditor today is also required to look into and comment upon the accounting policies followed by the management in the preparation of financial statements.

Accounting Standard-1 (AS1)

The view presented in the financial statements of an enterprise of its financial position and of Profit earned can be significantly affected by the accounting policies followed in the preparation of the financial statements. To appreciate the position presented, it is necessary to disclose the accounting policies adopted. The AS1 recommends the disclosure of certain accounting policies like foreign currency translation.

Some Indian enterprises are disclosing their accounting policies by way of a separate statement in their annual report to share holders but in many cases accounting policies are not fully and regularly disclosed. Many enterprises give the description of some of the accounting policies by way of foot note to the Balance Sheet.

Disclosure of the fundamental accounting assumption as their acceptance and use is not required but if they are not followed then the disclosure is must. e.g. the principles of going concern, consistency and accrual of revenues and cost.

The specific principles and methods adopted by an enterprise while preparing financial statements need to be disclosed. These different accounting policies adopted by different enterprises may be in different areas like (1) Methods of Depreciation (2) Treatment of expenditure during construction (3) Conversion of foreign currency (4) Valuation of inventory (5) Treatment of goodwill (6) Valuation of investment (7) Treatment of retirement benefits (8) Recognition of Profit on long term contracts (9) Valuation of fixed assets (10) Treatment of contingent liabilities etc.,

Disclosure of all significant accounting policies adopted in the preparation and presentation of financial statements shall form a part of the financial statements and should not be scattered over several statements, schedules and notes.

Any change in an accounting policy which has a material effect should be disclosed. The amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Of course, the disclosure of accounting policies cannot remedy a wrong or inappropriate treatment of the item in the accounts.



In short as per AS1, all accounting policies adopted in the preparation and presentation of financial statement should be disclosed.

Expenditure During The Period of Construction

Apart from the direct expenditure on fixed assets, which has to be capitalized, an enterprise incurs various other expenditures during the period of construction. The research committee of the ICAI, has published a report of the study on the accounting treatment of such expenditure.

According to this study –

- (1) A cut off date should be fixed to segregate expenditure during construction period from subsequent expenditure. It is on this date, that the project is officially recognized as being ready for commercial production i.e. the trial runs are completed and the project is capable of producing commercially feasible quantities.
- (2) The Selection of cut off date acquires specific importance due to the fact that there is often a delay between the date when the plant is ready for commercial production and the date of actual commencement of commercial production.
- (3) All expenditure, other than direct capital expenditure, should be debited to Profit & Loss account, once the plant is ready for commercial production since a delay in commencement of production after this date is neither related to the acquisition of fixed assets nor does it add to the utility thereof. However, depreciation on fixed assets need not be provided if the fixed assets are not utilized due to delay in commencement of production. In case, the delay in commencing production is prolonged, the expenses of this period may be treated as deferred revenue expenditure and be written off subsequently.
- (4) Preliminary project expenditure, incurred in connection with the preparation of project report, conducting feasibility studies and handling preliminary negotiations with foreign collaborators and government authorities should be capitalized as part of the indirect construction cost of the project. The amount of such expenditure is to be apportioned over the individual assets in an equitable manner.
- (5) Financial expenses like interest and commitment charges incurred during the construction period on loans for financing the construction of the project should be included in the capital cost of the projects as indirect construction cost. The cost of procuring loans or the interest paid to the Shareholders under Section 208 of the Companies Act, 1956 should also be treated in the same way. However, once the production starts, no interest or other financial expenses or any borrowings should be capitalized. Interest and other charges on loans taken for providing working capital during construction period should be treated as deferred revenue expenditure and be written off over a period of three to five years after the commencement of production.
- (6) Notional or imputed interest charges should not be capitalized since they are not incurred.
- (7) Indirect expenditure relating to the construction of the project should be capitalized or part of the construction cost if it is incidental to the construction activity. Thus, expenses on office incidental to construction should be apportioned over individual assets on equitable basis.
- (8) General expenses un-related to the construction activity, like expenses on staff training programmers, building up sales and office organization as also publicity and sales promotion campaigns should be treated as deferred revenue expenditure, to be written off within a reasonable period after the commencement of production.
- (9) Advance payments to contractors and others should not be shown under the specific fixed assets. These should be disclosed in the balance sheet under the general heading of “Fixed Capital Expenditure” or as separate item under the heading “Loans and Advances”.
- (10) Capital expenditure on incomplete construction work should be shown under the heading “Construction Work in Progress”. The complete unit of fixed assets should be shown in the accounts under the heading “Fixed Assets”. Any facilities or equipment built specially for the purpose of construction should be capitalized.
- (11) Abnormal losses during construction period should not be capitalized but should be written off over a period of 3-5 years after commencement of production.



- (12) Expenditure on commissioning the project including the cost of test runs and experimental production may be capitalized as an indirect construction cost.
- (13) The financial statement prepared during the construction period should contain appropriate disclosures of construction work-in-progress, fixed assets, advances to contractors, supplies & others, preliminary expenses and deferred revenue expenses.

6.4 ADJUSTMENTS FOR PREVIOUS YEAR

Adjustments for previous year for outstanding expenses like arrears payable to workers as a result of revision of wages with retrospective effect during the current period are made as usual and auditor has to verify it as a normal item, but in regard to income or expenses which arise in current year as a result of errors or omissions in the preparation of the financial statements of one or more prior periods, the provisions of AS-5 should be observed.

Errors in the preparation of the financial statements of previous year may be discovered in the current period. Errors may occur as a result of mathematical mistakes, mistakes in applying accounting policies, misrepresentation of facts or oversight.

Previous years items are normally included in the determination of net profit or loss for the current period. An alternative approach is to show such items in the statement of profit and loss after determination of current net profit or loss. In either case, the objective is to indicate the effect of such item on the current profit or loss.

6.5 PROVISIONS OF COMPANIES ACT, 1956 REGARDING ACCOUNTS

(A) Books of Accounts to be kept by Company (See-209)

Every company shall keep at its registered office proper books of accounts with respect to –

- (i) All sums of money received and expended by the Company and the matters in respect of which the receipt and expenditure take place.
- (ii) All sales and purchases of goods by the Company
- (iii) The assets and liabilities of the company and
- (iv) In the case of company pertaining to any class of companies engaged in production, processing, manufacturing or mining activities, such particulars relating to utilization of material or labour or to other items of cost as may be prescribed, if such class of companies are required by the Central Government to include such particulars in the books of accounts.

All these books may be kept at such other place in India as the BOD may decide and the company shall within seven days file with the Registrar a notice in writing giving full address of the other places.

Proper summarized returns at intervals of not more than three months are to be sent by the branches in or outside India to the company at its registered office or the other places.

The books kept by the company and its branches should give true and fair view of the state of affairs of the company or branch offices and should be kept on accrual basis and according to the double entry system of accounting.

The books of accounts and other books and paper shall be open to inspection by any director during business hour.

The books of accounts of every company relating to a period of not less than eight years immediately preceding the current year, including the vouchers relevant to any entry in such books of accounts shall be preserved in good condition. Any of the person who fails to take all responsible steps to secure compliance of the above by the company or has by his own willful act been the cause of any default by the company there under, he shall, in respect of each offence, be punishable with imprisonment for a term which may extend to six months or with fine which may extend to ten thousand rupees or with both.

(B) Inspection of books of account etc., of Companies (Section 209A)

The books of accounts and other books and papers of every company shall be open to inspection during business hours-



- (i) By the Registrar or
- (ii) By such officer of the Government as may be authorized by the Central Government in this behalf or
- (iii) By such officers of Securities and Exchange Board of India as may be authorized by it.

Such inspection does not require any prior notice to the Company. The Company should make available all such books etc., as required within such time and at such place as the person so specify. The Company should give all assistance in connection with the inspection.

The person making the inspection may get copies of accounting books etc., and also may place mark of identification thereon in token of the inspection have been made.

The person making inspection shall have the same powers as are vested in a Civil court under the Code of Civil procedure 1908 in respect of (i) the discovery and production of books of account and other documents at such place and such time as may be specified by such person (ii) summoning and enforcing the attendance of persons and examining them on Oath. (iii) Inspection of any books, registers and other documents of the Company at any place.

The person making inspection shall make a report to the Central Government or SEBI as the case may be. If default is made in complying with above provisions every officer of the company who is in default shall be punishable with fine which shall not be less than fifty thousand rupees and also with imprisonment for a term not exceeding one year.

Any director or officer convicted of an offence under this provision shall on and from that date of conviction be deemed to have vacated his office as such and on such vacation of office, shall be disqualified for holding such office in any company for a period of five years from such date.

(C) Annual Accounts and Balance Sheet (Section 210) -

At every Annual General Meeting the Board of Directors of the Company shall lay before the company a Balance Sheet and a Profit and Loss account for the financial year. The person who fails to take reasonable steps to comply with shall be punishable with imprisonment for a term which may extend to six months or with fine which may extend to ten thousand rupees or with both.

(D) Constitution of National Advisory committee on Accounting Standard (Section 210A)

The Central Govt. may, by notification in the official Gazette, constitute an Advisory Committee to be called the National Advisory committee on Accounting Standards to advice the Central Govt. on the formulation and laying down of accounting policies and accounting standards for adoption by Companies or class of Companies under this Act.

The Advisory Committee shall consist of the following members :-

- (i) A Chairperson, who shall be a person of eminence and well versed in accountancy, finance, business administration, business law, economics or similar discipline.
- (ii) One member each from ICAI, ICWAI and ICSI.
- (iii) One representative of the Central Govt. to be nominated by it.
- (iv) One representative of the R.B.I. , to be nominated by it.
- (v) One representative of the Comptroller and Auditor General of India, to be nominated by him.
- (vi) A person who holds or has held the office of Professor in accountancy, finance, business management in any University or deemed University.
- (vii) The Chairman of the Central Board of Direct Taxes
- (viii) Two members to represent the Chambers of Commerce and Industry to be nominated by the Central Government.
- (ix) One representative of the SEBI of India to be nominated by it.

The Advisory Committee shall give its recommendations to the Central Govt. on such matters of Accounting Policies and Standards and Auditing as may be referred to it for advice from time to time.

**(E) Forms and Contents of Balance Sheet and Profit and Loss Account (Section 211) –**

Every Balance Sheet of a Company shall give true & fair view of the state of affairs of the company as at the end of the financial year and shall subject to the Provisions of Sec. 211, be in the form set out in Part VI of Schedule I or as near thereto as circumstances admit or in such other form as may be approved by the Central Govt. either generally or in any particular case and in preparing the Balance Sheet due regard shall be had, as far as may be, to the general instructions for preparation for Balance Sheet under the heading “Notes” at the end of that Part I.

But this form does not apply to Insurance or Banking or Electricity Company etc., to which separate form is specified under the Act under which the company is formed.

Every Profit and Loss Account of a company shall give a true and fair view of the profit or loss of the company for the financial years and shall, comply with the requirements of Part II of Schedule VI.

Every Profit and Loss Account and Balance Sheet of the company shall comply with the Accounting Standards. If the company does not comply with the accounting standards, it shall disclose in its Profit and Loss Account and Balance sheet, the following –

- (i) The deviation from accounting standards
- (ii) The reasons for such deviation and
- (iii) The financial effect, if any, arising due to such deviation

The Balance Sheet and the Profit and Loss Account of a company shall not be treated as not disclosing a true and fair view of the state of affairs of the Company merely by reason of fact, that they do not disclose –

- (i) In the case of Insurance Company, any matter which are not required to be disclosed by the Insurance Act, 1938.
- (ii) In the case of Banking Company, any matter which are not required to be disclosed by the Banking Companies Act, 1949.
- (iii) In the case of a company engaged in the generation or supply of electricity, any matters which are not required to be disclosed by the Indian Electricity Act, 1910 and the Electricity (Supply) Act, 1948.
- (iv) In the case of company governed by any other special Act for the time being in force, any matters which are not required to be disclosed by the special Act, or
- (v) In the case of any company, any matter which is not required to be disclosed by virtue of the provisions contained in Schedule VI or by virtue of a notification.

Any person who fails to comply with the provisions of section 211 be punishable with imprisonment for a term which may extend to six months or with fine which may extend to ten thousand rupees or with both.

(F) Balance Sheet of Holding Company to Include Certain Particulars as to its Subsidiaries (Section 212)-

There shall be attached to the Balance Sheet of holding company the following –

- (i) The copy of the subsidiary company's Balance Sheet,
- (ii) The copy of the subsidiary company's Profit and Loss Account
- (iii) The copy of the subsidiary company's Board of Director's Report.
- (iv) The copy of the subsidiary company's Audit Report
- (v) The statement of the holding company's interest in the subsidiary
- (vi) When the financial years are different, the statement containing information about whether there has been any, and, if so, what change in the holding company's interest in the subsidiary between the end of the financial years of the subsidiary and the end of the holding company's financial year and details of any material change which have occurred between the end of the financial year or of the last of the financial years of the subsidiary and the end of the holding company's financial year in respect of
 - (a) The subsidiary's fixed assets
 - (b) Its investments
 - (c) The money lent by it
 - (d) The money borrowed by it for any purpose other than that of meeting current liabilities.



If any person fails to comply with the provisions of Section 212, he shall be punishable with imprisonment for a term, which may extend to six months or with fine which may extend to ten thousand rupees or with both.

(G) Financial year of holding company and subsidiary (Section 213)

Central Govt. may if it appears to it desirable, extend the financial year of Holding Company or subsidiary company so that the financial years of both the companies may end on same date on the application or with the consent of the Board of Directors of the company whose financial year is to be extended.

(H) Rights of Holding Company representatives & members (Section 214)-

A holding company may, by resolution, authorize representatives to inspect the books of accounts of its subsidiaries. Members of holding company may exercise their rights as conferred by Section 235 in respect of any subsidiary.

(I) Authentication of Balance Sheet and Profit & Loss Account (Section 215)

Every Balance Sheet and Profit and Loss Account of a company shall be signed on behalf of the Board of Directors, by Manager or Secretary and by not less than two directors of the company one of whom shall be a Managing Director but when there is only one of its directors for the time being in India, the balance sheet and Profit and Loss Account be signed by such director and an explanation to that effect explaining the reason for non compliance be attached to the Balance Sheet. In case of Banking companies it is signed by the persons specified under Section 29(2) of Banking Companies Act, 1949.

The Balance Sheet and Profit and Loss Account shall be approved by the Board of Directors before they are signed on behalf of the Board.

(J) Profit and Loss Account to be annexed and Auditors' Report to be attached to the Balance Sheet (section 216)

The Profit and Loss Account shall be annexed to the Balance Sheet and the Auditor's Report shall be attached there to.

(K) Boards Reports (Section 217)-

There shall be attached to every Balance Sheet laid before a company in General Meeting, a report by its Board of Directors, with respect to –

- (i) The state of company's affairs.
- (ii) The amount it proposed to carry to any reserves.
- (iii) The amount of dividend it recommends.
- (iv) Material changes affecting the financial position of the company, which have occurred between the end of the year and the date of the report.
- (v) The conservation of energy, technology absorption, foreign exchange earnings and outgo.
- (vi) The Director's Responsibility statement indicating that in the preparation of the annual accounts, the applicable accounting standards had been followed, selected accounting policies are applied consistently, proper and sufficient care taken for the maintenance of adequate accounting records etc.,

Any person, being a director of a company fails to take all reasonable steps to comply with the provisions of Section 217 be punishable with imprisonment for a term which may extend to six months or with fine which may extend to twenty thousand rupees or with both.

(L) Penalty for improper issue, circulation or publication of Balance Sheet or Profit & Loss Account (Section 218).

The Company and every officer of the company who is in default, shall be punishable with fine which may extend to five thousand rupees.

(M) Right of Member to copies of Balance Sheet and Auditor's Report (Section 219) –

Before 21 days of holding the Annual General Meetings, the copies of the Profit and Loss Account, Balance Sheets and Auditors Report be sent to each member of the Company, every trustee of debenture holders and to all person other than such member or trustee being persons so entitled.



On demand the company should provide the respective copies to the member of the company within seven days.

The officer and the Company in case of failure to comply with the provisions of Section 219 is punishable with a fine which may extend to five thousand rupees.

(N) Three copies of Balance Sheet etc., to be filed with the Registrar (Section 220)

Within thirty five days from the date of presenting before Annual General Meeting three copies of the Balance Sheet and the Profit and Loss Account signed by the Managing Director, Manager or Secretary of the Co. be filed with the Registrar. In case of default the company and every officer of the company who is in default shall be liable to like punishment as is provided by Section 162 for a default in complying with the Provisions of Section 159, 160 or 161.

(O) Duty of Officer to make disclosure of Payments etc., (Section 221) –

Where any particulars or information is required to be given in the Balance Sheet or Profit and Loss Account of a Company or in any document required to be annexed or attached thereto, it shall be the duty of the concerned officers of the company to furnish without delay to the company, and also to the company's auditor wherever he so requires, those particulars or that information in full as possible. This information may relate to payments made to any director or other person by any other company, body corporate, firm or person. If any person knowingly makes default in performing duty in this regard, he shall be punishable with imprisonment which may extend to six months or with fines which may extend to fifty thousand rupees or with both.

(P) Certain Companies to publish statement in the form in Table F in Schedule I (Section 223)

Every company which is a limited Banking company, an insurance company or a deposit, provident or benefit society shall before it commences business and also on the first Monday in February and the first Monday in August every year during which it carries on business, make a statement in the form in Table F in Schedule I or in form as near there to as circumstances admit.

A copy of the statement, together with a copy of the last audited Balance Sheet laid before the members of the company, shall be displayed and until the display of the next following statement, shall be kept displayed, in a conspicuous place in the registered office of the company, and in every branch office or place where the business of the company is carried on.

If default is made in complying with any of the requirement of section 223, the company and every officer of the company, who is in default, shall be punishable with fine which may extend to five thousand rupees for every day during which the default continues.

Of course, this section 223 shall not apply to a life assurance company or provident insurance society to which the provisions of the Insurance Act 1938 as to the Annual Statements to be made by such company or society, apply, with or without modification, if the company or society complies with those provisions.

6.6 STATISTICAL SAMPLING IN AUDITING

Sampling is the selection of a part of the population representing the total affairs. The term statistical “sampling” refers to the whole process of carrying out a test on a scientific basis.

This is framed in such a way to determine the degree of accuracy of a particular set of transaction rather than to discover individual errors. The ‘Statistical Sampling’ may be applied in auditing where in great number of transactions are involved e.g. Purchases, Sales, payrolls, salaries, inventories etc., Audit sampling is the application of a compliance or substantive Audit Procedure to less than 100% of the items within an account balance or class of transactions to enable the auditor to obtain and evaluate evidence of some characteristic of the balance or class and to form or assist in forming a conclusion concerning the characteristic, of course it should be noted that certain testing procedures do not come under this. Tests done 100% of the items within a population do not involve sampling, also the technique of selecting all items within a population which have a particular characteristic does not qualify on Sampling with respect to the portion of the population examined nor with respect to the population as a whole, since the items were not selected from the total population on a basis that was expected to be representative. Such items might have some characteristic of the remaining portion of the population but would not be the basis for a valid conclusion about the same.



At the time of actual start of audit the auditor has to decide whether all transactions be checked or only part of them be examined. If it is practicable to check each and every transaction then there is no need to think about statistical sampling. But in large scale organizations it would be almost difficult to check the huge volume of transactions due to the available limited time, that is why some kind of selective checking becomes inevitable. Effective auditing depends upon the proper selection of transactions.

Therefore, the auditor should be very careful at the time of selecting his audit samples and evaluating the results of audit procedure and hence he shall consider the time and efforts his staff can spend, past experience, the degree of confidence gained from few surprise sample checks, existence of internal control system and of internal auditing, Generally Accepted Accounting Principles and auditing standards while selecting audit samples.

The statistical sampling have advantage over judgment sampling as the statistical sampling provided mathematical base when judgment sampling is based on intuition. When an auditor is concerned with the design of compliance, the statistical sampling is appropriate.

The difference between the test check approach and the statistical sampling approach can be illustrated through the example of an auditor who wishes to obtain confirmation of debtors.

Suppose that there are 5000 debtors and that the internal control system has been found to be quite effective. If the auditor undertakes a test check, he may decide to obtain confirmation from ten percent of the total debtors. He would then prepare a list of 500 debtors.

It is quite likely that being in a hurry to complete the audit, he selects consciously or unconsciously only local debtor or those who he knows would reply. It could be that he included in his list the names of those debtors with whom he got acquainted during the examination of Sale invoices. In doing so he may be unconsciously leaving out those debtors whose accounts are static for a long time. Thus, his list may not be representative of the debtors as a whole.

Again when the confirmations are received, he would not be able to assess as to how far the confirmations from 500 debtors selected arbitrarily represent the truth of all debtors balances.

Suppose the same auditor decides to under take confirmation of debtors through statistical sampling and for this, he will first determine the size of the sample. Instead of just taking an arbitrary figure of 10%, he would determine the sample size through statistical tables. These tables show different sample sizes depending upon how confident the auditor wishes to be regarding the accuracy of his sample. The auditor would then select the debtor to be included in the sample on the basis of random number tables. Since he has to take only those accounts whose number is shown up by random number tables, there will be no element of bias in the sample and statistically the accounts so selected would be more representative of the debtor account as a whole. Once the confirmations are received from the sample debtors, the auditor can reach a more scientific conclusion with the help of statistical tables. This indicates that statistical sampling helps in a scientific verification of transactions on a selective basis.

While applying statistical sampling techniques for successful auditing the auditor should consider the following-

- (i) Use this technique only when the audit objective necessary so warrants depending on the circumstances.
- (ii) His opinion should be based only on the sample population.
- (iii) He should not be influenced by personal bias at the time of selecting samples.
- (iv) The Patterns in the population should not be permitted to influence the random of the sample.
- (v) He should base his estimates of maximum error rate on realistic grounds.
- (vi) He should not set un-realistic and unachievable goals.
- (vii) He should find out the reasons behind the variance after obtaining the sample results and then recommended corrective measures and express his opinions.

Designing Audit Samples –

Auditor should consider the following important factors at the time of designing the audit sample –

- (a) Audit objective
- (b) Population
- (c) Risk and Assurance



- (d) Tolerable error
- (e) Expected Error in the Population

(a) Audit Objective

First of all the auditor should think about the specific audit objective he is going to achieve, which will enable him to decide upon audit procedure. When, according to him, audit sampling is appropriate, the nature of audit evidence to be gathered and positive error conditions etc., relating to that evidence will help him in what population be selected for sampling as well as what constitute as error.

(b) Population –

The population is the entire set of data from which sample is drawn to reach a conclusion.

He should be careful while selecting sample that the population is appropriate to reach his audit objective.

(c) Risk and Assurance –

Auditor, while planning the audit uses his skill and judgment in assessing the level of audit risk, which include inherent risk, control risk and detection risk. Inherent risk and control risk remain irrespective of audit sampling procedures. He should consider detection risk arising from the uncertainties due to sampling. Sampling risk arises from the possibility that the auditors conclusion may be different from the conclusion based on entire population.

(d) Tolerance Error –

Tolerance error is the maximum error in the population which auditor accepts and still concludes that the results from the sample has achieved his audit objectives. For minimizing the tolerance error auditor has to select the larger sample size.

(E) Expected error in the population –

When auditor expects the presence of error, normally he examines a larger sample. Smaller sample sizes are justified in the case when the population is expected to be error free. To determine the expected error in population, the error levels found in previous audits, changes in accounting and other procedures adopted by the auditee and evidence available from evaluation of internal control system etc., proves useful.

Method of Sampling –

The sample selected should represent the population and for all items in the Population must have an equal opportunity of being selected.

The following are the common methods used for selecting the samples –

- (a) Random Number Selection
- (b) Systematic Selection Method
- (c) Haphazard Selection Method
- (d) Stratified Selection Method
- (e) Cluster Selection Method

(a) Random numbers Selection Method –

In this method, all items in the population have equal opportunity of being selected.

Under this method random number tables or computer generated random numbers are used.

(b) Systematic Selection Method –

Under this method, the first number is selected at random and then other numbers are selected using uniform interval for e.g. every ` 50,000/- in the cumulative value of the population is selected.

(c) Haphazard Selection Method

This method is an alternative to random selection method, here auditor draws a representative sample with no intention to either include or exclude specific items.



(d) **Stratified Selection Method**

Under this method the population is subdivided into sub population and all items in each sub-population have same characteristics and from each sub population samples may be drawn but auditor direct his effort toward the items which contains greater monetary error.

(e) **Cluster Selection Method**

In this method division of total items is made into sub groups and then at random few subgroups are selected entirely as samples.

Evaluation of sample Results

After verifying, examining, checking the sample selected the auditor should evaluate the sample results as under –

- (a) Analyze the error detected
- (b) Project the located error in sample to the population
- (c) Assess the sampling risk

(a) **Analyze the error detected**

The error found should be rechecked by using other method and after that the error still remains, auditor should treat the error as an error. He should also consider the qualitative aspects of the errors and the possible impact of error on other phases of audit.

(b) **Project the errors found in sample to the population –**

The auditor should project the error of sample to the population, where from the sample was drawn when number of subgroups are made, the projection errors is done separately for each sub-group and the results are accumulated.

(c) **Assessing the sample risk –**

The auditor should see whether error in population exceed the tolerance limit and for he should compare the projected population error to the tolerable error and also compare the sample results to the evidence gathered from other relevant audit procedures. If the projected error approaches tolerable error the risk incorrect acceptance increases, if the auditor determines that the risk is unacceptable he should extend his audit tests.

6.7 USE OF RATIOS AND PERCENTAGES FOR COMPARISON AND ANALYSIS TRENDS

A ratio is a quotient of two numbers and is an expression of relationship between the figures of two amounts. The relationship between the two accounting figures is known as accounting ratio. Thus, accounting ratios are relationship, expressed in Mathematical terms, between figures which have a cause and effect relationship or which are connected with each other in some other manner. Obviously no purpose will be served by working out ratios between two entirely unrelated figures, such as discount on debentures and sales. According to J. Batty, “the term accounting to ratio is used to describe significant relationships which exist between figures shown in a Balance Sheet, in a Profit and Loss Account, in a budgetary control system or in any part of the accounting organization.”. It indicates a quantitative relationship which is used for a qualified judgment and decision making.

The auditor can use ratio analysis to identify anything abnormal or anything which deviates from the expected and the known. Absolute quantity can be easily manipulated. However, it may be difficult to manipulate all the figures which are inter-related. Such manipulation normally causes widespread repercussions and can be detected easily. Ratio analysis is a useful tool for assembling the related but unorganised data into a meaningful and orderly pattern. By analysing the changes in the ratios and the trends so perceived, an auditor can spot variations in the normal pattern of transactions e.g. there is a direct relationship between the figures of gross profit and sales. The relationship would change if certain underlying business conditions change. Hence a change in the ratio of gross profit to sales in a particular year would indicate that either relevant business conditions have changed or that the figures are not reliable. Ratio analysis is thus a valuable tool, of overall assessment.



Ratio analysis only highlights symptoms. It is for the auditor to study the symptoms properly, correlate them and reach definite conclusions or identify for further enquiries.

Some of the common ratios are as under –

(A) Balance Sheet Ratios –

$$(i) \text{ Return on Investment} = \frac{\text{Net Profit before Interest and Taxes}}{\text{Net Capital Employed}}$$

$$\text{It can be split up} = \frac{\text{Net Profit}}{\text{Sales}} \times \frac{\text{Sales}}{\text{Net Capital Employed}}$$

$$(ii) \text{ Current Ratio or Working Capital Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

This indicates short term liquidity. An ideal current ratio is 2:1. The excessive current ratio is treated as a sign of managerial inefficiency. Window dressing or presence of mounting stocks may show a good current ratio. Low ratio shows the weak financial position.

$$(iii) \text{ Quick Ratio or Acid Test Ratio or Liquidity Ratio} = \frac{\text{Quick Assets (except stock \& Prepaid expenses)}}{\text{Quick Liabilities (except B.O.D.)}}$$

This indicates a short Term liquidity. Normally Quick Ratio should be 1:1. If there is a low quick ratio, the concern may be put into difficulties of the maturity date of quick liabilities.

$$(iv) \text{ Debt Equity Ratio} = \frac{\text{Owners Equity}}{\text{Debt Equity}}$$

This indicate a long term solvency. This ratio is acceptable as 1:1 Higher the ratio, the better would be the working capital position.

$$(v) \text{ Inventory to Working Capital Ratio} = \frac{\text{Stock at End}}{\text{Current Assets} - \text{Current Liabilities}}$$

The ratio is an index of the position of over stocking. It shows that the part of working capital is blocked in the closing stocks. The mounting stock represents the blocking of circulating assets.

(B) Income Statement Ratios :

$$(i) \text{ Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Net Sales}} \times 100$$

Low ratio would put the management into difficulties in the realization of fixed overheads. Low ratio indicates unfavorable purchasing polices, inability of management to develop Sales volume, over investment in plant facilities etc.,

$$(ii) \text{ Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Net Sales}} \times 100$$

It indicates operating efficiency. It is extremely useful to the management being an indication of cost control and sales promotion. This ratio is a guide to efficiency or otherwise of operating the business.

(iii) Expenses Ratios to Sales

$$\text{Material to Sales} = \frac{\text{Materials}}{\text{Sales}} \times 100$$

$$\text{Wages to Sales} = \frac{\text{Wages}}{\text{Sales}} \times 100$$



$$\text{F.O.H. to Sales} = \frac{\text{F.O.H.}}{\text{Sales}} \times 100$$

$$\text{Office expenses to} = \frac{\text{Office Expenses}}{\text{Sales}} \times 100$$

$$\text{Financial cost to sales} = \frac{\text{Tax provision} + \text{Debt Interest}}{\text{Sales}} \times 100$$

If these ratios are compared with ratios of previous year or with some other business organization, gives very important indication whether these expenses in relation to sales are increasing or decreasing or are stationary, which in its turn reflects the Profit earning Capacity of the concern. Lower the ratio, the greater is the profitability.

Combined Ratios :

$$(i) \text{ Inventory Turn over Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Average Inventory}}$$

A higher ratio suggests efficient business activity, while lower rates suggest that some steps should be taken to push up the sales. This ratio is used for measuring profitability. A low inventory ratio may reflect dull business, over investment in inventory etc.,

$$(ii) \text{ Turnover to total Assets} = \frac{\text{Sales}}{\text{Total Assets}} \times 100$$

This ratio is important measure of overall performance of the business. It aims to point out the efficiency or inefficiency in the use of total assets or capital employed.

$$(iii) \text{ Debtors Turn over Ratio} = \frac{\text{Total Debtors} + \text{BR}}{\text{Net Credit Sales}} \times 360$$

It is an index of the number of days for which the accounts of Debtor and Bills Receivable remained uncollected.

$$(iv) \text{ Account Payable to Turnover Ratio} = \frac{\text{Cr.s.} + \text{BOD} + \text{Other Current Liabilities}}{\text{Average net sales per month}}$$

This ratio shows what period will be required to retire the current liabilities at the current rate of turnover.

$$(v) \text{ Return of Total Assets and interest} = \frac{\text{Net Operating Profit Before Taxes}}{\text{Total Assets}}$$

This ratio measures the profitability of total assets. It is the significance of the employment of fixed assets and current assets in the business.

$$(vi) \text{ Return on Net Profit} = \frac{\text{Net Profit before Tax and Interest}}{\text{Total Asset} - \text{Current Liabilities}}$$

This ratio is intended to measure the earning power of the Net capital of the business.

Analysis has certain limitations like it concentrates on the past performance and deeds in aggregate and serves only as warning signs but though proves helpful in discovering trouble spots when applied in trend analysis. While using this technique auditor may use above ratios or other relevant ratios on the basis of his acquaintance with the clients business.



Following illustrations will explain the calculation of different ratios and drawing conclusions –

Illustration No. 1 : Following is the trading account of Mr. Niranjana for the year ending 31st March 2010 with the corresponding figures for the previous year.

Trading Account

2009 `			2010 `		2009 `	2010 `
12,500	To Opening Stock	13,300	60,000	By Sales		74,800
48,000	To Purchases	58,400	13,300	By Closing		
12,800	To Gross Profit	15,200		Stock		12,100
73,300		86,900	73,300			86,900

And, following is the Balance Sheet of Mr. Niranjana as at 31st of March 2010.

Liabilities	Amount `	Assets	Amount `
Premises 7,400		Plant and Machinery	14,000
Liabilities		Motor Vehicle	3,800
Capital 24,000		Stock	12,100
Add, Net profit 4,500		Debtors	502
Less, Drawings (6,000)	22,500	Bank Current A/c	650
Bank Loans	10,000	Cash in Hand	48
Creditors	6,000		
	38,500		38,500

Calculate –

- (i) Gross Profit Ratio
- (ii) Current Ratio
- (iii) Acid Test Ratio

And, answer the following –

- (i) Is Mr. Niranjana Solvent ?
- (ii) Is he over trading ?
- (iii) Is there fall or rise in Gross Profit ratio ?
- (iv) What can cause a rise or fall in the G.P. Ratio ?

Solution :

$$\begin{aligned}
 \text{(i) G. P. Ratio} &= \frac{\text{Gross Profit}}{\text{Sales}} \times 100 \\
 &= \frac{12800}{60000} \times 100 = @ 21.33\% \quad \text{2006} \\
 &= \frac{15200}{74800} \times 100 = @ 20.33\% \quad \text{2007}
 \end{aligned}$$



$$\begin{aligned}
 \text{(ii)} \quad \frac{\text{Current Ratio/Working Capital Ratio}}{\text{Capital Ratio}} &= \frac{\text{Current Assets}}{\text{Current Liabilities}} \\
 &= \frac{13,300}{16,000} \\
 &= 0.83:1 \\
 \text{(iii)} \quad \text{Acid Test Ratio / Liquidity Ratio} &= \frac{\text{Liquid Assets}}{\text{Liquid Liabilities}} \\
 &= \frac{12000}{6000} \\
 &= 0.5:1
 \end{aligned}$$

Answers to the queries raised –

- (1) Mr. Niranjana is not a solvent business man. The Solvency Ratio i.e. working capital Ratio and Acid Test Ratio, both are not satisfactory. The ideal working capital Ratio is 2:1 but here in this case the working capital Ratio is 0.83:1, it is too low. Hence, Mr. Niranjana may be put into difficulties at the maturity of current liabilities. The accepted Acid Test Ratio is 1:1, but here in this case it is 0.5:1. Indicating Mr. Niranjana is unable to meet his current liabilities out of his liquid funds immediately.
- (2) Over trading is the result of excessive Sales. Over trading is the curse to the business. Increasing tendency of Credit Sales, Piling of Stock, Price Spiral, reduction in turnover, poor Cash position are the signs of over trading. In overtrading credit period taken is more than normally allowed.
The over all liquidity declined and the net working capital position becomes precarious. There is increase in current liabilities to a great extent. These are the signs of overtrading. The above signs are applicable in the case of business man Mr. Niranjana. Hence Mr. Niranjana's business is over trading.
- (3) G.P. Ratio of 2009 is 21.33% and that of 2010 is 20.33%, hence we can conclude that there is a decrease in G.P. Ratio by 1%.
- (4) A Low Gross Profit Ratio may indicate unfavorable purchasing policies, inability of management to develop Sales volume, over investment in plant facilities etc.,

$$\begin{aligned}
 \text{(1)} \quad \text{Capital Gearing Ratio} &= \frac{\text{Share Holders Fund}}{\text{Fixed Income bearing loans}} \\
 \text{I Year} &= \frac{12,40,000}{11,00,000} = 1.14 : 1 \\
 \text{II Year} &= \frac{13,20,000}{8,00,000} = 1.53 : 1 \\
 \text{(2)} \quad \text{Total Investments to long term liabilities} &= \frac{\text{Share Holders fund \& Long Term Liabilities}}{\text{Long Term Liabilities}} \\
 \text{(i)} \quad \text{Year} &= \frac{23,40,000}{11,00,000} = 2.13:1 \\
 \text{(ii)} \quad \text{Year} &= \frac{20,20,000}{8,00,000} = 2.53:1
 \end{aligned}$$

Trend analysis – Trend analysis shows the relative changes between two or more periods. The trends are analyzed for each item of income and expenditure included in Profit and Loss account. The auditor uses this technique to detect unusual decline, to arrive at a conclusion before expressing his opinion in the Audit Report. This trend analysis involves (a) the selection of base period (b) the Computation of different percentages of the current years figures on figures of base year (c) The comparison of current years percentages with base year's percentages (d) the analysis of unusual changes in percentages of current year on the basis of base year's percentages.

The Trend analysis can be understood well from following illustrations –



Illustration No. 1 – As an Auditor give your Analysis and suggest auditing procedure in relation to the following:

Credit Sales for the year under consideration	25,00,000
Accounts Receivables at the end of the year	4,00,000
Day's Sales in Account Receivable during the last year.	44

Solution :

$$\text{Average Daily Sales} = \frac{(25,00,000)}{360} = ₹ 6,944$$

$$\text{Day's Sales in Account Receivable} = \frac{(4,00,000)}{6,944} = ₹ 57.60$$

$$\text{Previous year's Day's Sales in Account Receivable (given)} = ₹ 44$$

This shows that, during current year the Company is not collecting its receivables as rapidly as it did in the previous year. This increase in the day's Sale in account receivable indicates towards a signal that there is some problem in receivables collection, may be increase in bad debts or inefficiency of collecting machinery or wrong policies adopted by the management.

Auditing Procedure to be followed –

- (1) Auditor should review cash receipts and remittances advices for the subsequent period.
- (2) He should obtain credit reports on significant past dues.
- (3) He should analyze year end sales to determine any abnormal Sales, determine its nature and see whether properly recorded in relevant period.

6.8 INTERFIRM AND INTRAFIRM COMPARISON

Inter firm comparison is a technique of comparing the performance, efficiencies, costs and profits and various concerns in an industry for assessing its own performance and ascertaining the reasons for any difference in performances/efficiencies etc. Inter-firm comparison has been used on a large scale with the objective of making choice of investment by potential investors or to assess the stage of performance of a particular organisation vis-a-vis that of others. The British Institute of Management has explained this aspect as follows :

“Inter-firm comparison is concerned with the individual firm, its success and the part played by the management in achieving it. The end-product of a properly conducted inter-firm comparison is not a statistical survey but the flash of insight in the mind of the Managing Director of a firm which has taken part in such exercise. The results of this give him an instant and vivid picture of how his firm's profitability, its cost, turnover and other key factors affecting the success of a business compared with those of the other firms in this industry”.

The term intra-firm comparison means comparison of two or more departments or divisions belonging to the same firm with the objective of making meaningful analysis for the purpose of increasing the effectiveness or efficiency of the departments or divisions involved.

Thus both inter-firm and intra-firm comparison have the same objective with the difference that while the former compares the performance of the firm with other firms, the latter compares the performance of the firm within itself. The comparison may cover the financial position or operating results or both.

Inter-firm comparison, is one of the main techniques, available to management of the day for higher management control and planning. Progressive management always asks itself the questions.

- (1) How is our unit performing in comparison to that of others?
- (2) Are we operating as efficiently as we might?
- (3) Are there areas of our business where improvements might be made?
- (4) If we are successful, what are the 'strong points' on which our success depends?
- (5) How can we increase our efficiency and profitability?



Study Note – 7

COMPANIES ACT PROVISIONS RELATING TO AUDITS

This study note includes

- **Statutory Auditor – Appointment, Remuneration, Removal, Rights, Duties & Liabilities**
- **Joint Audit**
- **Branch Audit**
- **Audit Certificate**
- **Audit Report**
- **Relevant Provisions of the Companies Act, 1956 and the Income Tax Act 1961.**
- **Interface between Statutory Auditor and Internal Auditor.**
- **Corporate Governance**

7.1 STATUTORY AUDITOR

The Companies Act 1956 has made the audit of accounts of companies in India compulsory.

Section 224 to 233 B provided for the qualifications, disqualifications, appointment, removal, rights, duties, & liabilities of company auditors.

Qualification of Company Auditor

- (i) A person shall be qualified to be an auditor of a company, if he is a practicing Chartered Accountant within the meaning of the Institute of Chartered Accountants Act of India 1949.- **Sec.226(1)**
- (ii) A firm shall be qualified to be appointed as auditor of a companies, if all the partners of the firm are practicing Chartered Accountants within the meaning of Chartered Accountants Act 1949,- **Sec. 226(1)**
- (iii) A person holding a certificate in an erstwhile **part B** State Act 1951 which entitled him to act as an auditor of companies in the territories of that state, is also entitled to be appointed as an auditor of companies registered anywhere in India . **Sec.226(2)**
- (iv) A person shall be qualified to be appointed as an auditor to audit cost records maintained u/s 209 (1) (d) by the companies, if he is a practicing **Cost Accountant** within the meaning of Cost & Works Accountant Act, 1959. **Sec. 233 B.**
- (v) A firm shall be qualified to be appointed as cost auditor of company if all the partners of the firm are practicing **Cost Accountants** within the meaning of Cost & Works Accountants Act 1959 - **Sec.233 B**

COMPANIES ACT PROVISIONS RELATING TO AUDITS

Disqualification of Company Auditor

Certain persons and/or firms even if they are qualified as above or otherwise, are disqualified from being appointed as auditors of company—

- (i) Chartered Accountant from other countries not being a member of the ICAI – Sec.226 (1) inferred meaning.
- (ii) Cost Accountant from other countries not being a members of the ICWAI – sec. 233 B (inferred meaning).
- (iii) A body corporate –Sec.226(3) (a)
- (iv) An officer or Employee of the Company (b) Sec 226 (3) (b)
- (v) A person who is either a Partner or employee of an officer or employee of the company Sec. 226(3) (c)



- (vi) A person who is indebted to the company or has given any guarantee or provided any security in connection with the indebtedness of any third person for amount exceeding ` 1000 Sec. 226(3) (d)
- (vii) A person holding any security of that company after a period of one year W.E.F. 13.12.2000 - Sec 226 (3) (c)
- (viii) Other disqualification as per sec of the ICAI Act, 1949 (e.s. a person who is a minor, lunatic, convicted of guilty, insolvent)

A person who is disqualified as above is also disqualified for appointment to be an auditor of

- (A) it's holding Company
- (B) it's subsidiary company
- (C) a subsidiary of it's holding company. – Sec 226.(4)

In addition to above, if an auditor of a company holds audit of more than 20 companies (based on paid-up capital), he is deemed to be disqualified for appointment as an auditor of other companies – Sec.224 (1 - B)

If an auditor attains any disqualifications after his appointment he shall be deemed to have vacated his office as such – Sec.226(5)

Appointment of a Company Auditor

A person qualified to be appointed as an auditor of the company can be appointed as auditor of the company as provided by section 224 of the Companies Act, 1956.

The provision regarding appointment of Company Auditor can be explained as under-

(A) First Auditor:

The first auditors of the company is to be appointed by the Board of Directors within the period of 30 days from the date of incorporation of the company and he shall hold the office up to first Annual General Meeting. If the Board of Directors fails to appoint the auditor/s the first director the company in general meeting may appoint the first anditor/s. - sec.224(5)

(B) Appointment of Subsequent Auditors:

Every appointed auditor holds office till the conclusion of the Annual General Meeting and therefore, every Annual General Meeting has to appoint subsequent auditor. Immediately after receiving the intimation of appointment from the company, the auditor within 30 days intimate his acceptance or refusal of the appointment to the Registrar of Companies in form No-23-B

Usually, the retiring auditor shall be re appointed as an auditor of the company, except, when

- (i) He is not qualified for re- appointment or
- (ii) He has shown his unwillingness by way of a notice in writing to get reappointed or
- (iii) A Resolution, not appointing retiring auditor or to appoint somebody else in his place is passed by the company. – Sec.224(2)

(C) Appointment by Special Resolution :

In case of companies in which not less than 25% of the subscribed share capital is held whether singly or in any combination by—

- (a) A Public Financial Institution or a Government Company or Central Govt. or any State Govt. or any financial institution or other institution in which a State Government hold not less than 51% of the subscribed share capital, or
- (b) A nationalized bank or an insurance company carrying on general insurance business

The appointment or re- appointment of auditor under this section must be made by passing a special resolution. If company fails to pass a special resolution, it shall be deemed that, no auditor is appointed by the company,- Sec.224A.

(D) Casual Vacancy

Vacancy in the office of auditor caused by death, insolvency, or disqualifications of auditor can be filled up by Board of Directors of the company However, in case of vacancy caused by resignation of auditor is only to be



filled by general meeting of the company. An auditor appointed in casual vacancy shall hold office until conclusion of the next Annual General Meeting – Sec.224(6)

(E) Appointment by Central Government :

Where at an Annual General Meeting no auditor is appointed or reappointed the company must inform to the Central Govt. about it's failure within a period of 7 days. On receipt of information the Central Government may appoint a person to fill the vacancy in the office of auditor Sec.224(3) and 224 (4)

COMPANIES ACT PROVISIONS RELATING TO AUDITS

(F) Appointment of Auditor of Government Companies & Certain Other Co's

The auditors of Government Companies shall be appointed or reappointed by the Central Govt. on the advice of the Comptroller & Auditor General of India- sec.619, notwithstanding the provisions contained in section 224 & 233.

The provision of sec. 619 shall apply to a company, in which the Central Govt. or State Govt. hold either singly or jointly not less than 51% of the paid up share capital, be appointed or reappointed by the Central Govt. on advice of the Comptroller and Auditor General of India. (Sec. 619B)

(G) Appointment of Auditors in the case of a company in voluntary liquidation

No question of fresh appointment of auditors for this specific purpose envisaged by sec 224 of the Companies Act.1956.

But if the winding up proceeding continues for more than one year, then it is left to members or creditors, as the case may be, to decide whether or not the auditors are to be appointed to audit the liquidators account. (Sec.496)

Remuneration of Statutory Auditors

- (a) Remuneration of Statutory Auditor will be fixed by the directors when auditors are appointed by them before the first Annual General Meeting or to fill up a casual vacancy other than the one caused by the resignation by the auditor.
- (b) In case of the auditor appointed by Annual General Meeting, remuneration will be fixed by the shareholders.
- (c) In case of the Govt. Company Auditor, whose appointment is made by the Central Govt. the remuneration will be fixed by CAG.
- (d) In case of the Auditor appointed by AGM fixing of remuneration entrusted upon the Board. The Board of Directors will fix the remuneration.

For this purpose, the expression “remuneration” should be deemed to include any sums paid by the company in respect of the auditor's expenses.

Students may note that the Act does not specifically require that the remuneration should be fixed at the same meeting of the company at which the appointment is made. It may, therefore, be fixed at a subsequent meeting. Where a retiring auditor has been reappointed, his remuneration in the absence of any resolution fixing a different remuneration is considered to be the amount already fixed, in respect of the previous appointment.

Where, in addition to the normal audit, the auditor is also required to render services as may be required, he is entitled to receive remuneration in addition to the normal fee for the audit.

Such additional remuneration is a matter of arrangement with the directors. But any remuneration paid as fees, expenses or otherwise for such service must be disclosed in the Profit & Loss Account. The remuneration paid to the auditor is required to be shown in the Profit & Loss Account separately :

- (a) **As auditor:**
- (b) **As advisor or in any other capacity in respect of:**
 - (i) **Taxation;**
 - (ii) **Company law matters;**
 - (iii) **Management service; and**



(c) In any other manner (Sch. VI - Part - II - Clause 4-B)

The Council of the Institute of Chartered Accountants of India in the “Statement on Payment to Auditors for other Services” has recommended that the fees paid to the auditors for other services rendered should be disclosed in the Profit and Loss Account of the companies under the following head in order to give precise and correct information to the shareholders and others who read the accounts pertaining to—

- (i) Tax representation**
- (ii) Company law matters**
- (iii) Management services**
- (iv) Internal auditing**
- (v) Other services**

In case of joint audit, if other services were rendered by one of the joint auditors or in case of a company having a branch, the other services were rendered by the branch auditor disclosure should be made accordingly.

Removal of an Auditor

(1) First Auditor : By implication first auditor appointed by the Board of Directors can be removed by passing ordinary resolution in the first annual general meeting of the company. **Sec. 244(1)**

(2) Subsequent Auditors: The subsequent auditors can be removed either before the expiry of his office or after expiry of his office.

- (a) Removal Before Expiry of office:** If the company wants to remove the auditor before the expiry of his office, the company must obtain the prior permission of the Central Govt. and then give 14 days notice to shareholders of the company and copy of such notice shall be forwarded to the concerned auditor and the auditor may send his representation to the company.

The company on receipt of such representation either circulate it amongst the shareholders of the company or read it in front of general meeting. If the general meeting after considering his representation, passes a resolution, to remove the auditor, then the auditor stands removed from his office. **(Sec. 224(7) and Sec. 225)**

- (b) Removal After the Expiry of the office :** At every Annual General Meeting the office of the auditor expires and hence either the reappointment of retiring auditor or appointment of new auditor is necessary, usually the retiring auditor is reappointed, but if the company wants to remove the retiring auditor the company has to give 14 days notice to its members and forward its copy to the retiring auditor. The retiring auditor, if he so desires, send his representation to the company and the company on receipt of such representation may circulate it among its members or get it read in the meeting and if the meeting after considering the representations passes a resolution to remove the auditor, the auditor stands removed. **(Sec 224(7) and Sec. 225)**

Rights of Company Auditor

To enable the company auditor to perform his duties efficiently, **Sec.227** of the Companies Act 1956, has given some rights as well as imposed certain duties on company auditor. The provisions relating to rights can be explained as under-

- (A) Access to books of accounts & voucher etc :** Every auditor of the company shall have a right of access at all times to the books accounts, vouchers, records of the company, whether kept at the head office of the company or elsewhere. The auditor has a right to inspect books, accounts, vouchers and supporting documents at any time. This right of the auditor is absolute & unconditional and the same cannot be restricted by the company through its Articles of Association **(Newton VS Birmingham's Small Arms Co. (1906) 2ch 378)**
- (B) Obtain Information & Explanation :** Every Auditor is entitled to obtain all information & explanation necessary for his audit work from office bearer of the company. This power to obtain information is wide enough to cover any information or explanation at his discretion. If it is denied by any body, auditor may report it to the shareholders.
- (C) Report to members :** Company Auditor has right to communicate his comments & remarks to the members through his report complying with the provisions of the Companies Act and made thereunder.



- (D) **Receive Notice** : The auditor of the company has a right to receive all notices to any general meeting of the company.
- (E) **Attend General Meeting** : The company auditor has right to attend the general meeting of the company, as well as he can participate in the discussion relating to accounts & audit of the company as provided u/s 231.
- (F) **Branch Accounts**: Auditor, if he desires, can visit the branches & inspect the book of accounts of the branch as u/s 228 of the Companies Act.1956.
- (G) **Advice**: The auditor can take legal or technical advice relating to the accounts of the company & while reporting on the matters where in he has obtained such advice , he should clarify it but should give his own opinion & not that of the expert (**London & General Bank 1895.**)
- (H) **Lien**: The company auditor has right of lien on working papers, these are the property of the auditor & can retain the same with him, (**Chantrey Martin and Co. VS Martin 1953. 2 All ERG 91.**)
- (I) **Remuneration**: The auditor has a right to receive remuneration of the audit work completed by him. And also, if, he is removed during the year, he is entitled to a full years remuneration (**Homer VS Quilter , 1908.**)
- (J) **Signature**: The auditor has a right to sign the audit report as provided u/s 229 of the Companies Act 1956.
- (K) **Indemnity**: The Co. auditor has a right to be indemnified out of the assets of the company against any liability incurred by him in defending against any civil & criminal proceeding by the company if it is provided that the auditor worked honesty while performing his audit work, as per section 633.
- (L) **Correct Wrong Statement**: If the auditor 's advice to amend faulty P& L A/c . and/or Balance sheet ,not followed by the directors, he can report it to share holders by way of qualified report.

Duties of Company Auditor

The auditor owes large number of duties as explained below: -

(A) Duties to Share Holders:

- (i) **Report** shareholders about the true & fair state of affairs of the company u/s 227 (2)
- (ii) Ensure that the **Balance Sheet** and **Profit & Loss A/c** gives the required information as per sec. 227 (2)
- (iii) State in his report that he has obtained all the **necessary Information** u/s 227(3)
- (iv) State in his report that whether the Co. **has maintained** all required books of accounts u/s227(3).
- (v) Report whether the **Balance Sheet and Profit & Loss A/c agrees** with the books of accounts u/s 227 (3).
- (vi) State in his report whether the B/S and **Profit & Loss A/C** comply with the **Accounting Standards or not.**
- (vii) Give the reasons behind **qualifying** his report u/s 227(4)
- (viii) Report whether he has received the audit report on the **branch** accounts audited by other auditor & how he has dealt with the same in preparing his report u/s 227(3)
- (ix) Auditor shall state in his report whether –
 - (a) The **loans** are properly secured & the terms are not against the interest of the company.
 - (b) The **transactions** merely representing book-entries as recorded in the books are not against the interest of the company.
 - (c) The **securities** have been sold by Co.'s other than Banking Investment Co.', at a price-less than purchase price.
 - (d) **Loans** made by Co. have been shown as fixed deposits.
 - (e) **Personal expenses** have been charged to revenue account sec . 227(1-A)
 - (f) Report whether the company has complied the requirements of CARO-2003 (Sec. 227 (4A)

(B) Duties towards company :

- (i) **Prospectus**: Auditor has to certify profits or losses, assets & liabilities, dividend paid etc. disclosed in the prospectus (sec 56.)



- (ii) **Statutory Report:** Auditor has to certify the statutory Report of the company which requires to present it in its Statutory Meeting (sec. 165.)
- (iii) **Public deposits:** Auditor has to report about whether the Company has complied with the requirement, of RBI in regard to public deposits or not. (Sec. 58AA)
- (iv) **Signature** Auditor should sign the audit report prepared by him (Sec. 229.)
- (v) **Insolvency:** Auditor should make a report on the Company's Profit & Loss A/c. for the period from last audited P & L Account to the date of declaration required to be accompanied with the declaration of solvency by the company (sec 488(2).)

(C) Duties towards Government :

- (i) **CARO-2003:** It prescribes verification of large number of corporate activities & this order imposed various responsibilities on auditor & it is the duty of the auditor to verify the records of the company from these angles & ensure that the scarce resources of the company are properly utilized.
- (ii) **Investigation:** It is the duty of the company auditor to assist the investigator appointed by the Central Govt. u/237 to investigate into the matters regarding the affairs of the company.

(D) Duties towards general public :

- (i) Auditor has to bear in mind the interest of general public as his office is of public confidence & faith.
- (ii) While conducting audit he should see that his report does not fail to disclose material information, which may affect the company's state of affairs.
- (iii) While certifying prospectus he should see that it does not include misleading statements which may cause the general public to subscribe to the Company's share issue & may suffer a financial loss in future, (**Hadley Byrne & Co.LTD VS Hiller & Partners**)

Liabilities of Auditor

Auditor's liability is most dynamic & always changing from time to time. In past auditors were held liable to their principals only but now a days they are liable to third parties too. Auditors liabilities can be classified as under.

- (A) Liabilities for Negligence.
- (B) Liabilities under the Companies Act 1956
- (C) Liabilities for misfeasance.
- (D) Liabilities under Penal Code.
- (E) Liabilities under Chartered Accountants Act,1949 and under Cost & Works Accountants Act 1959. (under specific reference)
- (F) Liabilities under the I.Tax Act 1961.
- (G) Liabilities to the third parties.

(A) Liabilities for Negligence:

Negligence means carelessness, failure to use standard degree of care & skill while doing audit and whenever it is proved that auditor is guilty of negligence he is held liable to compensate the loss sustained by others , may be appointing company or any third party like Bank or I.Tax Deptt. as decided in the cases- **CANDLER VS Crane Christmas and Co. 1951.**

Hedlery Byrne and Co. LTD. VS Heller & Partners 1964.

Anns VS Merton London Borough Council.1978.

Junior Books Ltd. VS Veitsschi Co.Ltd.1982.

London Oil Storage Co.LTD.VS. Seear, Has Luck & CO.1904.

(B) Liabilities under Companies Act 1956

Sec. 62: Prospectus – Auditor is liable for certifying misleading statement in the prospectus and he has to compensate equivalent to damages suffered by the parsons (civil liability)



Sec. 233: Signing false report. or document- Auditor is liable for signing a false report or any other document u/s 227 & u/s 229 and if proved, he shall be punishable with fine which may extend to ` 10,000 (civil liability).

Sec 539 : Falsification of Books – If with intent to defraud or deceive any person, auditor of a company which is being wound up, destroys, alters, falsifies any books, papers or securities he shall be punishable with imprisonment for a term which may extend to seven years and shall also be liable to fine (Criminal liability).

Sec 628 : False Statement – If in any return, report, certificate, balance sheet, prospectus, statement or any other document required under Companies Act, a false statement is made and knowing it to be false, if auditor certifies it as true, he shall be punishable for a term which may extend to two years and shall also be liable to fine (Criminal Liability).

(C) Liabilities for Misfeasance:

The term misfeasance means breach of trust or duty and auditor is liable for equivalent damages suffered by the company to third party (Sec.543.) This liability was well decided in following cases-

The London & General Bank Ltd. 1895.

The Irish Woolen Co. Ltd. VS Tyson & Others 1900.

The City Equitable Fire Insurance Co. Ltd, 1925.

The West Minister Road Construction & Engg. Co.Ltd. 1932.

The Official Liquidator of Palai Central Bank Ltd. VS Joseph and others 1963.

(D) Liabilities under Indian Penal Code :

Auditor is liable under Indian Penal Code for frauds, furnishing false information etc.

Sec 177 : Prescribe simple imprisonment up to 6 months & fine upto ` 1000 for furnishing false information.

Sec 188 and Sec. 199: A false statement on oath & false declaration attracts criminal liabilities under these sections of Indian Penal Code and attracts imprisonment up to seven years & fine.

Sec 193: For giving false evidence in judicial proceedings attracts imprisonment up to seven years or fine or both.

Sec 197 Signing any certificate or documents knowing it to be false, attracts imprisonment upto seven years or fine or both.

In following cases auditor was held liable for criminal offences-

Forrows Bank Ltd.,1921

Official Liquidator Karachi Bank Ltd. VS The Directors Of Karachi Bank.

(E) Liabilities under Chartered Accountants Act , 1949 and Cost & Works Accountants Act 1959 :

(I) Chartered Accountants Act. 1949: For professional misconduct, the council may either withdraw the certificate of practice or remove name of the Chartered Accountant from it's Members Register or forward the case to the High Court.

(II) Cost & Work Accountants Act 1959 : For professional misconduct, the council may either withdraw the certificate of practice or remove name of the Cost Accountant from it's Members Register or forward the case to the High court.

(F) Liabilities under I.tax Act 1961:

Sec 288 : Authorized Representative : If an auditor or a person has been convicted of an offence connected with any I. Tax proceeding or on whom penalty has been imposed under I. Tax Act, shall be disqualified to act as a representative of an assesses for a certain period.

Sec 278 : FALSE REPORTS – If an auditor or a person who certifies or induces other person to make & deliver to the I. Tax authorities false accounts, reports certificates etc., he shall suffer be rigorous imprisonment and / or with fine.

Rule 12A : Chartered Accountant : If prepares false I. Tax Return of an assesses in the capacity of an authorized representative or prepares false tax audit report to be accompanied with the I.T Return, it attracts, punishment by way of rigorous imprisonment.

**(G) Liabilities to third party:**

- (i) Generally, it appears that as there is no **privacy** of contract between auditor & third party, he cannot be held liable and as he is never appointed by third party he has nothing to do with such a party & this was confirmed by the case of **Le Lievre & Dennes VS Gould 1893**.
- (ii) No doubt there is no privacy of contract, the third party can hold the auditor liable for any **fraud**.
- (iii) Auditor has **moral** responsibility to third party.
- (iv) If any body relying on the audited statement of a company, takes any decision & **suffers** any loss because such statements were false, the auditor will be responsible to them.
- (v) If auditor had authorized the issue of a prospectus containing misleading statements, he would be held liable for damages to third party, which has purchased the shares of the company on the strength of such a misleading statement even though there might not have been any privacy of contract between the auditor & the shareholder.

7.2 JOINT AUDIT

Two or more auditors are some times appointed, specially in the case of large concerns such as banking or insurance companies or where the regulations of the company require such appointment.

In the absence of specific provisions in the Companies Act 1956, The Institute of Chartered Accountants of India has issued a statement on the Responsibilities of Joint Auditors to provide a clear idea of the professional responsibilities under taken by the Joint Auditors.

According to the statement it would not be correct to hold an auditor responsible for the work of another and each joint auditor will be responsible only for the work allotted to him. In coming to these conclusions, the council considered that the extent of work to be carried out is a matter of professional judgment and that no two firms, whatever be their standing and competence, will necessarily exercise their judgment in an identical manner so as to perform the same volume of work in the same manner.

Where joint auditors are appointed, they should divide the work of audit between them by mutual discussion. Such division of work would usually be in terms of identifiable operating units or specified areas of work and, in such a case, it is a good practice to communicate to the client, wherever possible, the actual division of work.

Where auditors have been allotted the work of separate units or branch it would be desirable for each auditor to prepare a separate report on the financial statement of the branch or the unit for which he is responsible.

When a natural division of work is not possible, the statement suggests that some division of work, by classification of assets or liabilities or income or expenditure or period of time, should be made.

It is the responsibility of each joint auditor to determine the extent of audit test to be applied in relation to the area of audit allocated to him and the manner in which it is to be performed.

Consequently, it is the separate and specific responsibility of each joint auditor to enquire in to the review of the prevailing systems internal control relating to the work allocated to him.

Not with standing allocation of the job between the joint auditors on some agreed basis, it is possible that certain areas and matters may continue to be of common concern. Consequently, each auditor should bring to the attention of his co-auditors the matters which require discussion, the disclosure or application of judgment, by the submission of a report or a notice prior to the finalization of audit.

Each joint auditor is to assume that his co-auditor have carried out the audit in accordance with the auditing and assurance standards, laid down by the Institute.

It is not necessary for a joint auditor to review the work performed by his co-auditor or to perform any tests in order to ascertain whether the work has actually been performed.

Each auditor is entitled to assume that his co-auditors will bring to his notice any departure from the Generally Accepted Accounting Principles or any material error noticed in course of the audit unless corrective action has already been taken before the accounts are finalized.

Where separate financial statements of a branch or an unit are reported upon by one of the joint auditors, each joint auditor is entitled to assume that such financial statements comply with all the legal & professional requirements regarding the disclosures to be made and also present a true and fair view of the state of affairs of the unit audited.



As regards the report, where joint auditors are in disagreement with regard to the report, each one of them would be justified in expressing his own opinion through a separate report. Even when more than two joint auditors are appointed, there is no question of minority with regard to audit report.

It can be argued that though, in so far as the delimitation of professional responsibility is concerned the pronouncement has adopted a practical approach to the problems posed by joint audit, all the questions of practical relevance specially those relating to allocation of the audit work might not have been adequately answered. Accounting after all involve complex process. It may not be a simple proposition to rationally allocate the work and to ensure overall truth and fairness on the basis of piecemeal work carried out by different auditors adopting an equal standard. The statement also does not answer the question of civil liability of joint auditors to the client or the third parties.

For the purpose of computation of the number of company audits pursuant to the Sec 224 – IB of the Companies Act each joint auditorship in a company will be counted as one unit.

Advantages of Joint Audit

Joint Audit basically implies pooling together resources and expertise of more than one firm of auditors to render an expert job in a given time period which may be difficult to accomplish acting individually. It essentially involves sharing of the total work. This is by itself a great advantage. In specific terms the advantages that flow may be the following :

- (i) Sharing of expertise
- (ii) Advantage of mutual consultation
- (iii) Lower work load
- (iv) Better quality of performance
- (v) Improved service to the client
- (vi) Displacement of the auditor of the company often obviated.
- (vii) In respect of multinational companies the work can be spread using the expertise of the local firms which are in a better position to deal with detailed work and the local laws and regulations.
- (viii) Lower staff deployment cost
- (ix) Lower cost to carry out the work
- (x) A sense of healthy competition towards a better performance

Disadvantages of Joint Audit

The following may be the disadvantages of a joint audit

- (1) Sharing of fees
- (2) Psychological problem, where firms of different standing are associated in Joint audits
- (3) Superiority complex of some auditors may affect the work of co-auditor
- (4) Problem arises regarding co- ordination of the work
- (5) Areas of work of common concern being neglected
- (6) Uncertainty about the liability for the work done.

7.3 BRANCH AUDIT

In accordance with the principle of independent audit of the company accounts, the Companies Act in Section 228 has provided for the audit of accounts of branches. Section 2(9) of the Companies Act defines a branch office in relation to a company as :

- (i) any establishment described as a branch by the company; or
- (ii) any establishment carrying on either the same or substantially the same activity as that carried on by the head office of the company; or
- (iii) any establishment engaged in any production, processing or manufacturing but does not include any establishment specified in any order made by the Central Government under Section 8 of in Companies



Act (Viz. Branch Audit Exemption Rule) Section 228 of the Companies Act provides that where a company has a branch office, the accounts of that office shall be audited either by the company's auditor appointed u/s 224 or by another auditor possessing qualifications prescribed u/s 226. In the case of a branch situated outside India, any of the above or an accountant qualified to act as auditor in the country concerned can be appointed as the branch auditor.

The scheme of Section 228 presumes that normally the company auditor shall be appointed as the branch auditor. However a company may decide to have the branch accounts audited by a person other than the company auditor in a general meeting. In such a situation, the company is required to appoint the branch auditor out of the eligible categories in the same meeting or it has to authorize the Board of Directors to appoint one in consultation with the company's auditor appointed u/s 224 (Statutory Auditor).

The appointment of branch auditors in consultation with the company's statutory auditor should not be taken to mean that the statutory auditor is in any way taking responsibility in respect of the work done by the branch auditor. The provision regarding consultation with the statutory auditor only implies that statutory auditor should be satisfied that prima facie, he is not aware of any reason why the proposed auditor should not be appointed as branch auditor. The branch Auditor shall have the same powers and duties in respect of the audits of the branch accounts as the company auditor has in relation to the company accounts. The powers that the company auditor enjoys in relation to branch accounts are the rights

- (i) to have access at all times to the books of accounts and vouchers of the branch
- (ii) to visit the branch and
- (iii) to obtain information and explanation considered necessary for the audit of the branch accounts.

But the branch auditor, unlike the company auditor will not have the right to attend the general meeting of the company or to receive the notice and other related communications in connection with the general meeting. The branch auditor is required to prepare a report on account of the branch examined by him and forward the same to the company's auditor. It is obvious that when the company auditor himself is the auditor for the branch accounts, there cannot be any question of any report being made on the branch accounts audited. He, as the auditor for the company, is under duty to make a report on the consolidated accounts in accordance with Section 227 of the Companies Act.

The branch auditor shall receive such remuneration as may be fixed for him by the general meeting appointing him or by the Board of Directors, if so authorized by the General Meeting, subject to the terms and conditions specified. Naturally, it is reasonable to presume that the branch auditor will not necessarily hold office like the statutory auditors under section 224.

Though independent professional scrutiny of the branch accounts is the principle in providing audit, the legislature, having regard to the element of materiality and other considerations, has provided that under certain circumstances the accounts of the branch may not be audited. Companies (Branch Audit Exemption) Rules 1961 have been issued under sec 228 (4A) to provide for the exemptions, a branch of a company carrying on manufacturing, processing or trading activity, account for average quantum of activity not exceeding higher of ` Two lakhs or 2% of the average turnover of the company shall be exempt from the purview of audit of branch accounts.

Quantum of activity means the highest out of the following :-

- (i) the aggregate value of the goods or articles produced, manufactured , or processed or
- (ii) the aggregate value of the goods or articles sold and services rendered or
- (iii) the amount of the expenditure, whether of a revenue or a capital nature, incurred by a branch office during a financial year.

There may be exemption also on other grounds. But these exemptions are discretionary subject to the satisfaction of the Central Government viz :

- (i) If there are satisfactory arrangements for the scrutiny and check at regular intervals of the accounts of the branch office of a company, not carrying on manufacturing or processing or trading activities, by a person who is competent to scrutinize and check the accounts.
- (ii) If arrangements are made for the audit of the accounts of the branch office by a person possessing the qualifications necessary for appointment as branch auditor even though such person is an employee of the company.



- (iii) if a branch auditor is not likely to be available at reasonable cost, having regard to the nature and quantum of activity carried on at the branch or having regard to any other reason.
- (iv) If for any other reason, the Central Government is satisfied that exemption may be granted.

The company auditor in his report is to make a mention about exemption from audit granted to any of the branches of the Company under the Companies (Branch Audit Exemption) Rules, 1961

Company's Auditor in Relation to Branch Accounts, Branch Audit And Branch Auditor.

When the company's auditor himself is auditor for the branch accounts, he treats the whole company as audit unit and ensures that the branch accounts have been properly incorporated in the main office account for consideration. Also there remains no question of any separate and distinct right to visit branch or to have access to the books, accounts and vouchers.

When the branch accounts are audited by a person other than the company's auditor, it is necessary to define the position of the company auditor in relation to branch accounts and branch auditor.

The Companies Act, u/s 228 (2), has given a right of the company's auditor to visit the branch and to have access to the books of accounts and vouchers maintained at branch when the branch audit is conducted by a person other than the company's auditor. Also, the Companies (Branch Audit Exemption) Rules, 1961 has retained this right for the company's auditor in respect of branches granted exemption from audit – this is a right given to the company auditor and not a duty cast on him. If in his own assessments of the situation, he considers it necessary for the proper audit of the accounts of the company, he may visit the branch and may have access to the books, accounts and vouchers maintained there; but it is not compulsory that he must visit the branch or branches.

Under Section 228(3) (c), the company's auditor is required to deal with the branch audit report received from the branch auditor, in preparing his own reports. The manner in which to deal with report is left to him. This requirement is supplemental to the main duty cast on him under section 227(3)(bb) to state in his report whether the branch audit report has been forwarded to him and how he has dealt with the same.

Full freedom of judgment has been given to the company auditor to decide the prima facie relevance and impact of the branch audit report on the total company accounts. Certain matter may appear material and important in limited context of the operations of the branch may be considered not much significant in setting of total company accounts. He, therefore, may incorporate the points, if any, made in branch audit report if he considered the same relevant in making the Consolidated Accounts true & fair.

He at his discretion may drop any or all the qualifications made in the branch audit report.

However, if the branch audit report contains qualifications on matters specially required to be disclosed in the Companies Accounts pursuant to the Schedule VI requirement, then it is obvious that the company auditor is left with no choice but to incorporate them in his own report after confirming the accuracy of the report, if he so feels.

The Company's auditor has a certain measure of responsibility in respect of the accounts and papers of the branch. This is shown by the fact that he has a right to visit the branch and has access to the papers and documents he has to make disclosure of anything in regard to the branch which he thinks is not in order and which has come to his notice.

The Statutory Auditor and Branch Auditor and has come the conclusion that the Statutory Auditor would not be responsible in respect of the work entrusted to the branch auditor.

However, sufficient liaison between the two auditors is needed to ensure that the work is performed expeditiously, and expresses the view that statutory auditor will be within in his right to issue written communication to the branch auditor to that end.

The statutory auditors are entitled to make such enquiries as they think fit from the branch auditor. In making those enquiries, the statutory auditor will have regard to the materiality of the branch and any other circumstances affecting the operations of the company.

The auditor of the branch office should comply with request for information from the statutory auditors recognizing that such a request results not from a doubt as to competence of the branch auditor but for legal duty cast upon the statutory auditors to ensure that the accounts give a true and fair view and also gives information required by the Companies Act.



The statutory auditor may require the branch auditor to answer a detailed questionnaire regarding matters on which the statutory auditors required information that he considered necessary for an expeditious and proper audit but nevertheless keeps him free from any responsibility as regards the audit work performed by the branch auditor. In effect the statutory auditor is positioned to supervise to the branch auditor's work and to this extent, it is in his accordance with the provision of the Companies Act. It has however, absolved the auditor from any responsibility connected with the work supervised.

7.4 AUDIT CERTIFICATE

Some times apart from an audit report for general use, an auditor is often called upon to give a certificate for special purpose. The certificate should include the following :—

- (a) Auditor should see that there is a suitable **declaration** by the management about the subject matter.
- (b) Auditor should give the certificate on his **letter head** or on stationary carrying his name and address to avoid misunderstanding .
- (c) Auditor should clearly state his **limitations** and indicate the extent to which he has relied upon a technical expert if any.
- (d) Auditor should indicate the specific **record** covered by the certificate.
- (e) Auditor should mention the **manner** in which the audit was conducted.
- (f) Auditor should indicate in the certificate if he has made certain fundamental **assumptions**.
- (g) Auditor should make a reference to the information and **explanations** obtained.
- (h) Auditor should give clear **title** to it, indicating whether it is a report or a certificate.
- (i) Auditor should mention whether he has used any general purpose statement like Profit & Loss Account for his investigation and also, state whether that general purpose statement has been audited by **other auditors**.
- (j) Auditor should be careful while interpreting any law related matter, he should clearly mention that he is expressing merely his own **opinion**.
- (k) Auditor should see that the certificate should be **self contained** documents.
- (l) Auditor should clearly mention the **responsibility** assumed by him.
- (m) Auditor should, if he has referred the audited statements, clearly mention that the figures are used from the audited statements and relied upon.
- (n) Auditor should address the certificate to the client or the Public Authority or the person requiring it as the case may be. In appropriate circumstances it may be issued by using the words as **“to whom so ever it may concern “** .

Examples and Specimens of Auditor Certificates—

There are many more circumstance, where for, auditor is called for issuing a certificate, e.g.,

- (i) “Deposits Return” Certificate.
- (ii) “Ability to Refund Depositors” Certificate.
- (i) **Deposits Return Certificate** : As provided under rule 10(1) of the Companies(Acceptance of Deposits), Rules , a non banking, non financial company has to file periodical return in prescribed form containing the information about deposits accepted and the copy of the return is required to be filed with the R.B.I. This return is to be certified by the Company Auditor.



The specimen of the Certificate may be as under :-

CERTIFICATE

We certify that to the best of our knowledge and according to the information and explanation given to us and as shown by the records examined by us, the figures of deposits and interest rates under parts A, B and C of the return of the Co.Ltd. are correct.

We further certify the correctness of the particulars of the paid up capital and free reserves etc. given in the manager's certificate.

Signature & Seal of

Date:

Chartered Accountant /Cost Accountant

Place:

Full Address

- (ii) Ability to Refund Deposits Certificate:** As per the provisions of the Non Banking Financial Companies(Reserve Bank)Directions, issued from time to time every non banking financial company is required to furnish to the RBI a certificate from its auditor to the effect that, the full liabilities to the depositor of the company including interest are properly reflected in the Balance Sheet and that the company is in a position to meet the amount of such liability to the depositors. As prescribed by the RBI, the certificate shall be in following format—

CERTIFICATE

We certify that, on the basis of the checks carried out by us and the information and explanations given to us , I am of the opinion that full liabilities to the depositors of the company including interest payable thereon have been reflected in the financial statements as on 31st March..... of the company, as per the said financial statements and on a going concern basis and based on information and explanation given to me, is in a position to meet the liabilities to the depositors, as on that date.

Also, an auditor is required to give certificate under various provisions of the Companies Act 1956, for example, u/s 56 for matters in the prospectus, U/s 58 A for public deposits, U/S 165 for accuracy of the statutory report, etc.

In short, Audit Certificate is a written confirmation of the accuracy of the information stated therein but does not involve any opinion.

Signature & Seal of

Date:

Chartered Accountant /Cost Accountant

Place:

Full Address



7.5 AUDIT REPORT

Audit Report –

While conducting every audit auditor has to go through three phases-

- (a) Preliminary work for audit.
- (b) Conduct of actual audit, and
- (c) Conclusion of audit, which means submission of Audit Report.

Therefore, Audit Report is called as the ultimate and final product of every audit.

The meaning of Audit Report can be well understood from the following selected definitions-

LanCester – “A Report is a statement of collected & considered facts, so drawn up as to give clear and concise information to persons who are not already in possession of the full facts of the subject matter of the report.”

J.B.Ray - “The Report shall either contain an expression of opinion regarding the financial statements, taken as a whole or an assertion to the effect that an opinion cannot be expressed when an overall opinion cannot be expressed, the reason therefore should be stated. In all cases, where auditor’s name is associated with financial statements the report should contain a clear cut indication of the character of the auditor’s examination, if any, and the degree of responsibility he is taking.”

In short, the Audit Report is nothing but a statement of observation gathered & considered while proving conclusive evidence of company’s financial position. It is a medium through which an auditor expresses his opinion on the financial statement under audit. It is an important part of the audit as it provides the results of the audit conducted by the auditor.

5.1.2. Importance of Audit Report-

1. An Audit report is the end product of the auditing and is very important & concluding part of the audit process.
2. Audit report gives the auditor’s opinion on the accounts & record of the company, as examined by him.
3. Audit Report reflects the work done by the auditor.
4. Audit report is the instrument which, measures the auditor’s responsibility in regard to the true & fairness of the financial statement of the company.
5. Audit Report indicates the real position of the financial status of the company & which is used by different people as a reliable document.

Contents of Audit Report

The Audit report generally shows the nature and scope of audit conducted by the auditor and his opinion on the final accounts of the company. Companies Act, 1956 and International Auditing Guideline has laid down certain guidelines relating to the contents of auditing reports as under –

1. **Title** – The report has certain title like “Audit Report” to enable the readers to identify the report & distinguish it from reports issued by others.
2. **Address** – The audit report should appropriately be addressed e.g. in case of company audit, it should be addressed to the shareholders.
3. **Observations**–
 - (a) Auditor should state whether he has obtained all the information & explanations which to the best of his knowledge & belief were necessary for the purpose of his audit.
 - (b) He should state whether proper books of accounts as required by law have been kept by the company or not.
 - (c) He should mention whether Balance Sheet and Profit & Loss Account are attached there to give a true & fair view of the state of affairs of the company.
 - (d) He should state whether the Balance Sheet and Profit and Loss Account annexed there to are in agreement with the books of accounts.



- (e) He should state whether the Balance Sheet and Profit & Loss Account read with notes there on give the information in the manner required by the Companies Act. 1956.
 - (f) He should also, state whether the provision of section 227(1A) and 227(4A) of the Companies Act, and also that of a CARO are complied with or not and gives separate statement on that to form part of the audit report.
4. **Auditing Standards :** In the audit report the auditor should make a reference to the Standard on Auditing (SA) to ensure that he has carried out the audit in accordance with the established standards.
5. **Opinion:** The Audit Report should clearly set forth the auditors opinion on the company's financial position and operational results like "the Financial Statements give true & fair view of the state of affairs." The opinion may be either i) Unqualified ii) Qualified iii) Adverse or Negative iv) Disclaimer
- (i) **Unqualified :** When an auditor gives an opinion without any reservation, it is an unqualified opinion.
 - (ii) **Qualified:** When an auditor gives an opinion with certain reservation, it is said that he has given a qualified opinion.
 - (iii) **Adverse or Negative:** When an auditor states that he does not agree with the true & fair state of affairs exhibited by the final accounts, then it is an adverse or negative opinion.
 - (iv) **Disclaimer:** When an auditor states that he is unable to express an opinion as he has not received necessary evidence to form an opinion then it is a disclaimer of opinion.
6. **Signature:** The audit report is required to be signed in the name of the firm of auditors or the personal name of the auditor or both as appropriate, in keeping with terms of appointment (whether on Individual or a firm)
7. **Auditor's Address:** The report should contain the auditor's postal office address.
8. **Date of the Report :** The auditor report should carry the date of the report.

Qualified Audit Report

When auditor gives his report with certain reservations, then the report is called a qualified audit report. In following circumstances the auditor has to qualify his report.

- (a) He cannot conduct audit satisfactorily due to non availability of certain **books of accounts** or records, information or explanations necessary for conduct of his audit.
- (b) He finds that the **Balance Sheet** and Profit & loss Account have not been prepared in accordance with accepted accounting principles.
- (c) He detects that **provisions** for Bad & Doubtful Debts, Depreciation etc. are not adequate.
- (d) He detects that the company has created certain **secret reserve**.
- (e) The stock in trade has been **valued** at market price which is more than cost price.
- (f) He finds that the **contingent liability** for bills discounted has not been disclosed.
- (g) If in his opinion provision for **taxation** made is not proper.
- (h) When he finds any embezzlements of cash or misappropriation of goods or manipulation of accounts which considerably affects the financial position of the company.

Specimen of Qualified Audit Report:

Auditor's Report

To the Members of ABC Ltd.

1. We have audited the attached balance sheet of ABC Ltd. as at March 31, 2010 and also the Profit and Loss Account and the Cash Flow Statement for the year ended on that date annexed thereto. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.



2. We conducted our audit in accordance with auditing standards generally accepted in India. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
3. As required by the Companies (Auditor's Report) Order, 2003 issued by the Central Government of India in terms of Sub-section (4A) of Section 227 of the Companies Act, 1956, we annex hereto a statement on the matters specified in paragraphs 4 and 5 of the said Order.
4. Further to our comments in the Annexure referred to in paragraph 3 above, we report that :
 - (a) We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purposes of our audit;
 - (b) In our opinion, proper books of account as required by law have been kept by the Company so far as appears from our examination of those books;
 - (c) The Balance Sheet, Profit and Loss Account and Cash Flow Statement dealt with by this report are in agreement with the books of account;
 - (d) In our opinion, the Balance Sheet, Profit and Loss Account and Cash Flow Statement dealt with by this report comply with the Accounting Standards referred to in subsection (3C) of section 211 of the Companies Act, 1956;
 - (e) On the basis of written representations received from the directors and taken on record by the Board of Directors, we report that none of the directors is disqualified as on March 31, 2010 from being appointed as a director in terms of clause (g) of sub-section (1) of section 274 of the Companies Act, 1956;
5. Subject to the reservations noted below, in our opinion and to the best of our information and according to the explanations given to us the accounts give the information required by the Companies Act 1956, in the manner so required and give a true & fair view, in conformity with the accounting principles generally accepted in India.
 - (i) The sum of ` 20,00,000 has been advanced to a director of the company in contravention of the companies Act 1956.
 - (ii) The provision for bad & doubtful debts has been understated by ` 50,00,000
 - (iii) The contingent liability for bills discounted for ` 6,00,000 has not been disclosed.
 - (iv) The provision for I.Tax payable is made short by ` 19,00,000.

Gokul
May 1 , 2010

Sd/-
DEF

Partner
XYZ & Co.
Chartered Accountants

Clean or Clear or unqualified Audit Report

When auditor doesn't insert any reservation or qualification in his audit report then it is called a clean or unqualified audit report. As provided u/s 227 (2) of the Companies Act 1956, certain questions which the auditor of the company must inquire and report on specified issues in his audit report. When these questions are answered positively without qualification and also, the Balance Sheet and Profit & Loss Account exhibits true and fair view of the state of affairs of the company, the auditors gives a clean or unqualified report.



Specimen of Clean or Unqualified Report

Qualification in The Auditor's Report

The statutory provisions in the Companies Act relating to qualifications in the Auditors Reports are contained in section 227(4) of the Act which provides that where the Auditors are required, in their report, to answer any of the statutory affirmations in the negative or with a qualification, their report shall state reasons for such an answer. It is therefore, necessary for the auditor's to give the reason for any qualifications or reservations in his report. Beyond this, the Companies Act does not mention anything about the form and manner of qualification in the audit report.

In a majority of cases the auditors report on the accounts examined by them are found to be unqualified. This is due to the fact that the right of a statutory auditors to make a qualified report is a great deterrent, and prevents the managements of companies from resorting to accounting principles and methods of disclosure which are not in accordance with the law. The result is that the auditor of a company is in a position to persuade the management of the company to accept his views and modify the accounts or make such disclosure as are required by the law, as in the absence of these he would qualify his report.

A qualified report is not necessary unless the issues involved are material. However, items requiring disclosure under the law, such as the director's remuneration, whether material or not, have to be specifically disclosed. If this is not done, it is the duty of the auditor to qualify his report. (Sch. (VI) Part I, II & III)

Further, as an auditor is appointed by the shareholders to perform certain statutory functions and duties, it is expected of him that he will in fact perform these function and duties by following what is known as "generally accepted procedure of audit".

Aspects to be Considered in Qualifying Audit Report

While qualifying a report, it is important to :

- (i) Ascertain the various items the statement of fact and opinion referred to above) that required a qualification.
- (ii) Realize whether the auditors are in active disagreement with something which has been done by the company or merely unable to form an opinion, say, for lack of adequate information about an item.
- (iii) Establish whether the matters in question are so material as to affect the presentation of a true and fair view of the state of the affairs of the company, or are of such a nature as to affect only a particular item disclosed in the account; and
- (iv) See whether the matters constituting the qualification involved a material contravention of any requirements of the Companies Act which have a bearing on the accounts.

In a majority of cases, item which are the subject matter of qualification are not material as to affect the truth and fairness of the whole of the Accounts but merely create uncertainty about a particular item. In such cases, it is possible for the auditor to report that, in their opinion, but subject to the specific qualification mentioned, the accounts present a true and fair view. Sometimes however, the items which are the subject matter of qualifications are so material that it would be meaningless to state that, subject to the qualification, the accounts disclose a true and fair view. An extreme example would be where the auditors were not able to examine a substantial part of the books of account, e.g. when they were in police custody. In such case, it would not be proper to express an opinion on the truth and fairness of the accounts after stating that the books of accounts were not examined. In such cases the auditors must report that either :

- (i) They are unable to state whether the accounts present a true and fair view; or
- (ii) Makes a categorical statement that in their opinion the accounts do not present a true and fair view.

Which of the above two alternatives should be followed would depend upon the facts of each case.

Finally, the auditor of well established principle that they must give full information about the subject matter of the qualification and not merely create grounds for suspicion or inquiry and leave it to the shareholder to call out the facts by diligent inquiry. The distinction between "information" and "means of information" made in the London and General Bank's case is still valid.



Nature of Auditor's Opinion

An opinion must be unqualified or adverse. An auditor may also be unable to express an opinion. In many cases an opinion may be limited only to certain aspects.

Where an auditor gives an opinion on the various matters without any reservations. It is an unqualified opinion. An example of an unqualified opinion would be a statement by the auditor that "in our opinion and to the best of our information and according to the explanation given to us, the Balance Sheet and the Profit and Loss Account give a true and fair view of the state of affairs and working results....". In the case of companies in India, if the auditor makes the various statutory affirmations without reservations, he is said to have given an unqualified opinion. In practice a large number of audit reports of public limited companies contain unqualified opinions. This is probably due to the fact that the right of the auditor to qualify his report, often persuades the managements to agree to the modifications in disclosed accounts as suggested by the auditors.

Qualified Opinion

Where an auditor gives an opinion subject to certain reservations, he is said to have given a qualified opinion. A qualified opinion implies that the auditor states that the financial statements reflect a true and fair view subject to certain reservation. Thus, an auditor may give his particular objection or reservation in the audit report and state, "Subject to the above, we report that the Balance Sheet shows a true and fair view", where an auditor has no alternative but to give a qualified opinion, he must clearly express the nature of the qualification in his report. The reasons of the qualification should also be stated. In the case of companies, this is a legal requirement under section 227(4) of the Companies Act, which provides that, where the auditors answer any of the statutory affirmations in the negative or with a qualification, their report shall state the reasons for such answers. And to the extent possible indicate the financial implication on the Statement of Account of the year under report and in the following/subsequent years.

Adverse or Negative Opinion

An auditor gives an adverse opinion when he states that the financial statements do not represent a true and fair view of the state of affairs and the working results of the company. An adverse opinion is appropriate where the reservations or the objections of the auditor are so substantial that he feels that the accounts do not give a true and fair view. Where the auditor gives an adverse opinion he should disclose all the material reasons therefore.

Disclaimer of Opinion

Where an auditor fails to obtain sufficient information to warrant an expression of opinion, he can give a disclaimer of opinion. Accordingly, the auditor may state that he is unable to express an opinion because he has not been able to have sufficient evidence to form an opinion on the financial statements. An example of the disclaimer of the opinion can be a statement by auditor that, " we have been unable to state that whether the Balance Sheet shows a true and fair view.....". The necessity of disclaiming an opinion may arise due to many reasons. In certain circumstances the auditor may not get access to all the books of account for certain reasons. There may also exist very material items, the value of which may be totally uncertain. In many cases certain material information or explanations may not be forthcoming. Wherever an auditor disclaims an opinion he should give reasons for the same.

Difference between Audit Report and Audit Certificate

- (i) **Meaning** : Audit Report is a statement of collected and considered information so as to give a clear picture of the state of affairs of the business to the persons who are not in possession of the full facts. While Audit Certificate is a written confirmation of the accuracy of the information stated there in.
- (ii) **Opinion** : Audit Report contains the opinion of the auditor on the accounts, while Audit Certificate does not contain any opinion but only confirms the accuracy of the figures with the books of accounts.
- (iii) **Basis** : Audit Report is made out on the basis of information obtained & books of account verified by the auditor, while Audit Certificate is made out on the basis of the particular data capable of verification as regards accuracy.



- (iv) **Guarantee** : Audit Report may not guarantee correctness of financial statement in absolute terms, while Audit Certificate guarantees absolute correctness of the figures & information mentioned in the certificate.
- (v) **Coverage** : Audit Report always covers entire accounts of the concern, while Audit Certificate covers only certain part of the accounts of the concern.
- (vi) **Responsibility** : Audit Report does not hold auditor responsible for any thing wrong in the accounts, while Audit Certificate makes an auditor responsible if any thing mentioned in the certificate found as wrong later on.
- (vii) **Suggestion** : Audit Report may provide certain suggestions for improvement while Audit certificate does not provide any such suggestion.
- (viii) **Nature** : Audit Report is based on the vouching & verification of books of accounts, voucher, assets & liabilities, while Audit Certificate is based on checking arithmetical accuracy of the facts.
- (ix) **Scope** : Audit Report covers all transactions done during the year, while the Audit Certificate is very specific.
- (x) **Characteristics** : Audit Report is subjective as it is opinion oriented, while Audit certificate is objective as it is fact oriented.
- (xi) **Form** : Audit Report is required to be presented in the prescribed format, while Audit Certificate, except in few cases, is not required to be presented in any standard format.
- (xii) **Address** : Audit report is addressed to the members of the company at large or appointing authority, while Audit Certificate is addressed to particular person or sometimes may include the words like “ To Whomsoever it may concern”.

7.6 RELEVANT PROVISIONS OF THE COMPANIES ACT, 1956 AND THE INCOME TAX ACT 1961

(I) Appointment and Remuneration of Auditors Section 224.

- (1) In each Annual General Meeting auditor is appointed and within seven days the appointed auditor is to be intimated; before that a written certificate indicating that the appointment is within the limits of sub-section 224 (1B)
- (1A) Within 30 days of the receipt of the intimation of appointment the auditor should inform the Registrar of Companies in writing his acceptance or refusal.
- (1B) No company or its Board of Directors can appoint or reappoint a person who is in full time employment elsewhere or a person or a firm is holding appointment as auditor of 20 companies in case of companies each of which has a paid up share capital of less than ` 25 lakhs or 20 companies in other cases where in companies having more than 25 lakhs paid up capital does not exceed 10. The number of companies shall be counted by taking into account the companies where audit is under taken singly or jointly with any other person. The ceiling of 20 companies does not apply to the private companies since 13.12.2000.
- (1C) The auditor whose limit is expired should within 60 days of the intimation of appointment inform the company and Register his unwillingness to accept of the appointment
- (2) In any Annual General Meeting a retiring auditor shall be reappointed unless he is not disqualified otherwise.
- (3) If Annual General Meeting fails to appoint or reappoint an auditor, the Central Govt. may appoint a person to fill the vacancy the company within seven days of the AGM give notice to the Central Govt. about non- appointment of an auditor, otherwise every officer of the company who is in default shall be punishable with fine.
- (4) The first auditor of a company shall be appointed by the Board of Directors within one month of the registration of the company and the auditor so appointed shall hold office until first AGM. In AGM new auditor may get appointed. If Board of Director fails to exercise its power the company in general meeting may appoint the first Auditor.



- (5) The BOD may fill any casual vacancy in the office of an auditor but if the vacancy is caused by the auditor's resignation, it will be filled only in general meeting. The auditor so appointed will hold the office until the conclusion of next AGM.
- (6) Any auditor may be removed before the expiry of his term by the company in general meeting after obtaining previous approval of the Central Govt.
- (7) The remuneration of an auditor appointed by the BOD or Central Govt. may be fixed by the BOD or Central Govt. In the case of an auditor appointed by the Comptroller and Auditor General of India under section 619 shall be fixed by the company in general meeting and in case of other auditors by the members.

(II) Auditor not to be appointed except with the approval of the company by special resolution in certain cases – section 224A

- (1) In case of a company in which not less than 25 percent subscribed capital is held by any Govt., Govt. Company, Financial Institutions, Nationalized Bank or Insurance Company, then the auditor in AGM will be appointed by special resolution.
- (2) If the company fails to pass the resolution in the AGM, then the Central Govt. will make the appointment.

(III) Provision as to resolutions for appointing or removing auditor section 225

- (1) Special notice by a member u/s 190 shall be required for appointment of auditor other than retiring or providing expressly that the retiring auditor shall not be reappointed.
- (2) On receipt of notice of such a resolution, the company shall send its copy to the retiring auditor.
- (3) On receipt of representation from the retiring auditor, the copy of it be sent to every member of the company and if it is not sent, then it shall be read out at the meeting.
- (4) The above provisions shall apply to a resolution to remove the first auditor.

(IV) Qualifications and disqualifications of Auditors u/s 226

- (1) He must be a Chartered Accountant with in the meaning of Chartered Accountant Act 1949. A firm of C.A. is also qualified for appointment provided all the partners practising in India are qualified as aforesaid.
- (2) Holder of a certificate granted under a law provided all the partners practising in India an gratified as aforesaid (restricted states)
- (3) None of the following person shall be qualified for appointment as Company Auditor
 - (a) a body corporate
 - (b) an officer or employee of the company
 - (c) a person who is a partner or employee of an officer or employee of company.
 - (d) a person indebted to the company for an amount exceeding ` 1000
 - (e) a person holding any security of the company
- (4) A person who is not qualified for appointment as an auditor of the company, also not qualified for such appointment of the subsidiary company or holding company of such company or subsidiary of it's holding company.
- (5) If after appointment the auditor becomes disqualified he shall be deemed to have vacated his office as such.

(V) Powers and Duties of Auditors Section 227

- (1) Every Auditor shall have a right of access at all times to the Books of Accounts etc of the Company whether kept at head office or elsewhere.
- (2) Auditor shall make a report to the members, whether the Balance Sheet gives a true & fair view of the state of affairs of the company and the Profit and Loss Accounts give a true and fair view of the profit or loss.



- (3) Auditor in his report shall state whether he has obtained all required information and explanations and whether the company has maintained proper Books of Accounts as required by the law, whether the report on the audit of a branch, not audited by him is received by him or not, whether the Balance Sheet and Profit and Loss Account is in agreement with the Books of Accounts of the company, whether the P&L account & Balance Sheet comply with the Accounting Standards, whether any director is disqualified from being appointed as director etc.
- (4) If the answers to above are negative, the auditors report should contain the reasons thereof.
- (4A) The Central Govt. may by general or special order direct that the auditors report shall also include a statement on such matters or may be specified in the order. (CARO, 2003)

(VI) Audit of accounts of a branch office of company

- (1) Accounts of company's branch be audited by Companies Auditor or by a person qualified to be appointed as company auditor or by a person qualified under the local law in case of foreign branch.
- (2) In case branch accounts audited by other auditor, the Company Auditor is entitled to visit the branch office and has a right to access all books of accounts, records etc of the branch.
- (3) The Branch auditor be appointed in AGM or by the BOD if authorized by the AGM with consultation of company's auditor. The branch auditor shall have the same powers and duties as the Company Auditor has, he should send a report on the audit of the branch to the Company's Auditor. The remuneration and the tenure of his office will be fixed by the AGM or BOD if authorized so.
- (4) The Central Govt. may give exemption to any branch from the provisions of this (section.)

(VII) Signature of Audit Report etc. (section 229.)

Only the person or a partner of the firm of Chartered Accountants appointed as Auditor may sign the Auditor's Report or any other document of the company required by law to be signed by the auditor.

(VIII) Reading and Inspection of Auditor's Report (section 230)

The auditors report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

(IX) Right of Auditor to attend General Meeting (section 231)

Auditor has a right to receive the notice and related documents of general meeting and is entitled to attend the meeting and being heard as any part of the business concerns him as auditor.

(X) Penalty for non compliance with section 225 to 231 (section 232)

If default is made by a company in complying with the above provisions the company and every officer of the company who is in default shall be punishable with fine.

(XI) Penalty for non-compliance by auditor with section 227 and 229- (section 233)

If any auditors report is made or any document is signed otherwise than in conformity with the requirements of section 227 and 229; the auditor concerned and the person, if any, other than the auditor who signs the report or document, shall if the default is willful, be punishable with fine.

(XII) Power of Central Govt. to direct special Audit in certain cases – (section 233A)

- (1) If in the opinion of the Central Govt, the company's affairs are not being managed in accordance with sound business principles or prudent commercial practice or if the company is managed in such a way that it will cause a serious injury or damage to the interest of trade, industry or business, the financial position is such as to endanger it's solvency, the Central Govt. may at any time by order direct a special audit by a person whether in practice or not or by the company's auditor.
- (2) The auditor appointed above is termed as a special auditor.
- (3) The special auditor have the same power and duties as an auditor of a company, but he is required to submit his report to the Central Govt. instead of the members.
- (4) The special auditor's report include all the details as that of Company Auditor's Report and also on the matters specified by the Central Govt.



- (5) The Central Govt. may direct any person to provide all required information to the special auditor and in case of failure the person shall be punishable with a fine.
- (6) On receipt of the special Auditor's Report the Central Govt. may take such action in accordance with the provision of Companies Act or any other law for the time being in force.
- (7) The expenses including special auditor's remuneration be determined by the Central Govt. and payable by the company and in default of such payment shall be recoverable from the company as an arrears of land revenue.

(XIII) Audit of Cost Accounts in certain cases (section 233 B)

- (1) If Central Govt thinks it is necessary, may order the audit of Cost Accounts of a company which is required to maintain Cost Accounts u/s 209(1)(d) by a Cost Accountant.
- (2) The auditor under this section shall be appointed by the BOD of the company with the previous approval of the Central Govt. Before appointment the company shall get a certificate from the auditor that if the appointment made it is in accordance with the provision of section 224(1B).
- (3) The Cost Audit is in addition to that conducted by an auditor appointed under section 224.
- (4) The Cost Auditor has same powers & duties as that of Company Auditor and shall make his report to the Central Govt. in such form and within such time as may be prescribed and also send a copy of the same to the company.
- (5) A person referred under section 226(3) and (4) shall not be appointed or re- appointed as Cost Auditor.
- (6) It is company's duty to give all facilities and assistance to the person appointed for conducting the Cost Audit.
- (7) Within 30 days of the receipt of the Cost Audit Report the company shall furnish the Central Govt. with full information and explanation on every reservation or qualification contained in such report.
- (8) After the receipt of the Cost Audit Report and Company's explanation, the Central Govt. can call any further explanation and information within such prescribed time.
- (9) After receipt of above explanation etc. the Central Govt. may take such action on the report in accordance with the provision of the Companies Act or any other law for the time being in force, as it considers necessary.
- (10) The Central Govt. may direct the company whose Cost Accounts have been audited to circulate to it's members, along with the AGM notice, the whole or such portion of the said report as directed.
- (11) If default is made in complying with the above provisions the company and every officer of the company shall be liable to be punished with fine and fine with imprisonment respectively.

(B) Provisions of the Income Tax Act, 1961

1. Audit of accounts of certain persons carrying on business or profession- section 44(AB)

Every person if his total sales or gross receipts exceeds ` 40 lakhs in any previous year

Or

Carrying on profession if his gross receipts exceeds ` 10 lakhs in any previous year

Or

Carrying on business, the profit and gains from the business are 'deemed' on presumptive basis to be the profit of such person who is engaged in the business of civil construction or supply of labour for civil construction or owns and ply for hiring not more than 10 goods carriages, engaged in retail trade, engaged in the business of providing service in connection with production of mineral oil or foreign company engaged in civil construction or erection of plant and machinery if claimed income lower than the profit or gains so deemed to be the profit and gains of business in any previous year.

Get his accounts of previous year audited by Chartered Accountant before specified date and furnish the report of such audit in the prescribed form duly signed and verified by the Chartered Accountant.

The provision does not apply to Non resident assessee engaged in the business of operation of ships or operation of air crafts.



In the case where the assessee is required to get his accounts audited under any other law, it shall be sufficient compliance with the provision of Income Tax Act, if the audit is completed before the specified date and the report is furnished by that date along with a further report in prescribed form under signature of a Chartered Accountant.

2. Report from an Accountant to be furnished by persons entering into international transaction- section 92E

Every person who has entered into an international transaction during a previous year shall obtain a report from a Chartered Accountant and furnish such report before specified date in the prescribed form duly signed and verified in the prescribed manner by such C.A. and setting forth such particulars as may be prescribed, otherwise it will attract penalty u/s 271 BA.

3. Maintenance and audit of accounts of shipping companies section 115vw

An option for tonnage tax scheme shall not have effect in relation to a previous year unless such company

- (i) Maintain separate books of accounts in respect of the business of operating qualifying ships and
- (ii) Furnishes, along with the return of income for the previous year, the report of a Chartered Accountant, in the prescribed form duly signed and verified by such Chartered Accountant.

7.7 INTERFACE BETWEEN STATUTORY AUDITOR AND INTERNAL AUDITOR

In accounting matters the internal auditor and the statutory auditor operate in the same field. Both would have a common interest in determining that there is –

- (i) An effective system of internal control to prevent or detect errors and frauds and that it has been operating efficiently.
- (ii) An adequate accounting system to generate information for preparation of true and fair financial statements.

However, there are fundamental difference between the two forms of audits in terms of the status, responsibility, approach and scope of operation of an internal auditor and a statutory auditor.

- (a) **Status and Scope :** The internal auditor is a representative of the management and the nature and scope of his operations are determined by the needs and perception of the management. The statutory auditor on the other hand is independent of the management, his scope of operations and rights and duties are defined by the statute.
- (b) **Approach :** The statutory auditors approach would be governed by the duty placed on him to satisfy himself that the accounting statements presented to the shareholders shows a true and fair view of the profit and loss during the year and of the state of affairs of the company as on the date of the Balance Sheet.

The internal auditor on the other hand would operate with a view to ensuring that the accounting system is efficient and that the accounting information presented to the management are correct and disclosed material facts.

- (c) **Responsibility :** The internal auditor is responsible to the management who is his master. The statutory auditor is on the other hand is responsible directly to the shareholders. The internal auditor has not got the independent status like the statutory auditor.

The technique of audit adopted by both the auditors are common such as –

- (i) Verification of internal control system to see whether it is sound in principle and effective in operation
- (ii) Verification of accounting records and statements.
- (iii) Verification of assets and liabilities.
- (iv) Statistical comparison, enquiry etc.

- (d) **Appointment :** The appointment of the internal auditor depends entirely on the wishes of the management. The management may not have own internal audit. After promulgation of the CARO, 2003 it is obligatory



for certain companies to have internal auditor. It is obligatory for the statutory auditor to comment in respect of certain companies as to whether they have internal audit system commensurate with its size and nature of business.

The qualification of the internal auditor is not guided by any statutory provision. This is determined by the management.

As regards the internal arrangements between the statutory auditor and the internal auditor in the performance of their respective duties, reference may be made to SA-610 "Using the Work Internal Auditors" issued by the Institute of Chartered Accountants of India. The role of the internal audit function within an entity is determined by the management and its prime objective differs from that of the external auditor who is appointed to report independently on financial information. Nevertheless, some of the means of achieving their respective objective are often similar and thus much of the work of the internal auditor may be useful to the external auditor in determining the nature, timing and extent of his procedures. Thus, before deciding to place reliance upon the work of the internal auditor, the statutory auditor should, as part of his audit, make a general evaluation of the internal audit function. Such evaluation will help him in deciding to what extent he can rely upon the internal auditor's work and whether he may adopt less extensive procedures than would otherwise be required. In this connection, the statutory auditor should consider the following aspects :-

- (a) Status of the internal auditor in the organization-to whom does he report- whether any constraints or restrictions placed upon his work by management- whether he is free to communicate with the statutory auditor.
- (b) Scope of the internal auditor's function and whether recommendations of the internal auditor are acted upon.
- (c) Technical competence of the person carrying out the internal audit work.
- (d) Exercise of such professional care regarding internal audit work- whether there has been proper planning, supervision, review and documentation of internal audit work.

Considering the results of general evaluation of the internal audit function, the statutory auditor may decide to rely upon the internal auditor's work. It would be helpful if the statutory auditor ascertains the tentative plan of internal audit for the year and discusses the same with the internal auditor.

However, the degree of reliance that a statutory auditor can place on the work done by the internal auditor is a matter of individual judgment.

Finally, it must be emphasized that the report of the statutory auditor is his sole responsibility and that responsibility is not by any means reduced because of the reliance he placed on the internal auditor's work.

7.8 CORPORATE GOVERNANCE

Corporate governance is the manner of governing a company, corporate governance is the "mantra" of Board managed Corporate. Although as a principle it goes beyond merely complying with the legal procedure under the corporate and regulatory bodies, on paper it has remained as a procedure and compliance oriented concept.

Clause 49 of the Listing Agreement of SEBI requires listed companies to comply with certain conditions of "Corporate Governance" and to obtain a certificate from its statutory auditor regarding such compliance. This certificate is required to be annexed to the director's report and is to be sent to the stock exchange along with the annual return.

Report on Corporate Governance

- (i) There shall be a separate section on Corporate Governance in the Annual Report of company, with a detailed compliance report on Corporate Governance. Non Compliance of any mandatory requirement with reasons there of and the extent to which the non mandatory requirements have been adopted should be specifically highlighted.
- (ii) The companies shall submit a quarterly compliance report to the stock exchanges within 15 days from the close of quarter in the prescribed form. The report shall be signed either by the Compliance Officer or the CEO of the company.



For examining compliance with the above requirements the auditor should examine the

- (i) Minute book of Board of Directors
- (ii) Minute book of General Body Meeting
- (iii) Minute book of Audit Committee
- (iv) Corporate Governance Report
- (v) Mandatory Annual intimations filed by each director about the Directorships in other companies
- (vi) Consistency of segment wise information with the segment information disclosed in financial statements in accordance with AS 17.
- (vii) Discussion on internal control system and their adequacy and consistency with the opinion expressed by him under CARO, 2003.

The Auditor, in this regard, is required to issue his certificate as follows, as suggested by the ICAI.

CERTIFICATE

To,

The members of the _____ Co. Ltd We have examined the Compliance Condition of the Corporate Governances, stipulated under clause 49 of the listing agreement of the said company with the _____ Stock Exchange, by the _____ Co Ltd, for the year ended on _____.

The Compliance of Conditions of Corporate Governance is the responsibility of the management, our examination was limited to procedures and implementation there of, adopted by the _____ Co. Ltd for ensuring the compliance of the conditions of the Corporate Governance. It is neither an audit nor an expression of opinion on the financial statements of the _____ Co. Ltd.

In our opinion and to the best of our information and according to the explanations given to us, subject to the following

- (a) _____
- (b) _____

We certify that the _____ Co. Ltd. has complied with the Conditions of Corporate Governance as stipulated in the above mentioned Listing Agreement.

We state that out of _____ no of investors grievance _____ are pending for a period exceeding one month against the _____ Co. Ltd as per the records maintained by the Share Holders/ Investors Grievances Committee.

We further state that such compliance is neither an assurance as to the future viability of the _____ Co. Ltd nor the efficiency or effectiveness with which the management has conducted the affairs of the _____ Co.Ltd.

Place : _____

Date : _____

For and behalf of XYZ and Company

Chartered accountants

Partner/ Proprietor



Study Notes – 8

REVIEW AND AUDIT OF INTERNAL CONTROL SYSTEM

This study note includes -

- **Nature and Scope of Internal Auditing, Financial versus Operational Audit, Concepts of Efficiency Audit, Propriety Audit, Voucher Audit, Compliance Audit, Pre and Post Audits, Audit in depth.**
- **C. A. R. O.**
- **Internal Auditing Function**
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- **Detailed checking versus Sampling plans, Flow Chart Technique**
- **Internal Control, Nature and Scope, Internal Auditor and Internal Controls**
- **Field work collecting evidences, interviews, memorandum**
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- **Communications in Internal Auditing.**
- **Scope of Audit Committee**
- **Internal Audit and Investigation of fraud**

8.1 NATURE AND SCOPE OF INTERNAL AUDITING

NATURE OF INTERNAL AUDITING

The Institute of Internal Auditors has defined Internal Audit as - Internal Auditing is an independent appraisal activity within an organization for the review of operations as a service to management. It is a managerial control which functions by measuring the effectiveness of other control.

There are various definitions of Internal Auditing prevailing, which can be stated as follows:-

1. Internal Audit is a management tool, performed by employees of the organization to ensure correctness in accounting data and to detect fraud by way of periodical review of organizational system and procedures.
2. Internal Audit is a continuous and systematic process of examining and reporting the operations and records of a concern by its employees or external agencies specially assigned for this purpose. It is, in essence, auditing for the management and its scope may vary depending upon the nature and size of the concern.
3. It is a control system concerned with examination and appraisal of other control mechanisms.
4. Internal Audit is an extension of and as such is complimentary to Statutory Audit.

In short Internal Audit means appraisal of control techniques employed by a firm and its performance.

Necessity of Internal Audit to Management

Internal Audit has become an important management tool for the following reasons :-

1. It ensures compliance of Companies (Auditors Report) Order 2003.
2. Internal Auditing is a specialized service to look into the standards of efficiency of business operation.
3. Internal Auditing can evaluate various problems independently in terms of overall management control and suggest improvement.



4. Internal Audit's independent appraisal and review can ensure the reliability and promptness of MIS and the management reporting on the basis of which the top management can take firm decisions.
5. Internal Audit system makes sure the internal control system including accounting control system in an organization is effective.
6. Internal Audit ensures the adequacy, reliability and accuracy of financial and operational data by conducting appraisal and review from an independent angle.
7. Internal Audit is an integral part of "Management by System".
8. Internal Audit can break through the power ego and personality factors and possible conflicts of interest within the organization.
9. It ensures compliance of accounting procedures and accounting policies.
10. Internal Auditor can be of valuable assistance to management in acquiring new business, in promoting new products and in launching new projects for expansion or diversification of business.

Scope of Internal Auditing

The Institute of Internal Auditors defines scope of internal auditing as "The examination and evaluation of the adequacy and effectiveness of organisation's system of internal control and the quality of actual performance. Therefore, internal auditing is concerned with an evaluation of both internal control as well as the quality of actual performance.

According to The Institute of Internal Auditors, internal audit involves five areas of operations, which can be discussed as follows :-

- (a) **Reliability and Integrity of Financial and Operating Information** :- Internal Auditors should review the reliability and integrity of financial and operating information and the means used to identify, measure, classify and report such information.
- (b) **Economical and Efficient Use of Resources** :- Internal Auditor should ensure the economic and efficient use of resources available.
- (c) **Compliance with Laws, Policies, Plans, Procedures, Regulations** :- Internal Auditor should review the systems established to ensure compliance with those policies, plans and procedures, law and regulations which could have a significant impact on operations and should determine whether the organization is in compliance thereof.
- (d) **Accomplishment of Established Goals for Operations** :- Internal Auditor should review operations, programmes to ascertain whether results are consistent with established objectives and goals and whether the operations or programmes are being carried out as planned.
- (e) **Safeguarding of Assets** :- Internal Auditor should verify the existence of assets and should review means of safeguarding assets. The business transactions of an organization may be broadly divided into phases.
 1. **Planning stage** : It usually culminates in an authorization from the appropriate level of management in the organization. At this stage, the decisions are issues like whether or not to make or buy, whether or not to undertake a new project or export etc. These are more of managerial decisions and the scope of internal audit is often not much practical, in the initial stage unless it takes to what is called management audit.
 2. **Execution Stage** : This stage is the stage of recording in the various books of accounts, which only for correctness and classification of expenditure under the same heads as those mentioned in the project report. At this stage the scope of internal audit emerges out of need for correctness of accounts and proper classifications of heads in a designed manner.
 3. **Reviewing Stage** : The third and final stage deal with reviewing the transaction and here internal audit is intimately concerned. At this stage internal audit embraces the following main functions :-
 - (a) Scrutiny of the records of an undertaking to assess the reliability of the information contained therein.
 - (b) Examination of the documentary evidence from which the records are written up.
 - (c) Detection and prevention of error and fraud
 - (d) A general examination of the financial statements prepared from the records to ascertain whether a true and fair view has been given about the financial position at a specific date.



Internal auditing therefore, is a function distinct from authorization and recording. It is concerned not only with examination of the transaction as recorded in the Books of Accounts but also with appraisal of procedure with a view to effecting change for better efficiency, where possible.

A proper organizational status for the Internal Auditing Department ensures its relative independence so that it can carry out its work freely and objectively and render impartial and unbiased reporting. The functions, responsibilities and authority of the Internal Auditing Department should be clearly and specifically laid down in a written document. The Chief Internal Auditor should have a direct communication with the Board of Directors, or CEO.

He should submit periodic reports to the Board highlighting the various significant audit findings.

Financial Audit and Operational Audit

Financial Audit

The Institute of Internal Auditors has defined financial audit as under :-

“Financial Audit is a historically oriented, independent evaluation performed by the internal auditor or the external auditor for the purpose of attesting to the fairness, accuracy, and reliability of the financial data, providing protection for the entity’s assets; and evaluating the adequacy and accomplishment of the system (internal control) designed to provide for the aforementioned fairness a protection. Financial data, while not being the only source of evidence, are the primary evidential source. The evaluation is performed on a planned basis rather than a request.”

Financial Audit takes care of the protective aspect of the business and it does not normally carry out any constructive appraisal function of the business operations. It helps in detection and prevention of fraud. It also verifies whether documentation and flow of activities are in conformity with the internal control system introduced and developed within the organization. It helps coordinating with statutory auditor to help them in proper discharge of their function. Besides, financial audit also ensures compliance with statutory laws especially in financial and accounting matters.

Operational Audit

Operational Audit has been defined by the Institute of Internal Auditors as follows “an Operational Audit is a future oriented, independent, and systematic evaluation performed by the internal auditor for management of the organizational activities and controlled by top, middle and lower level management for the purposes of improving organizational profitability and increasing the attainment of the other organizational objectives, achievement of programmes, purpose, social objectives and employees development areas in which efficiency and effectiveness may be improved and identified and recommendations made that are designed to enable realization of the improvements. The measure of effectiveness includes both an evaluation of compliance with prescribed entity, operational policies and of the adequacy of them. Financial data may be a source of evidence, but the primary source is the operational policies as related to the organizational objectives. Operational Audit is a scientific tool and technique adopted by the auditor in progressive business concern with the following objectives :-

- (i) To ensure that operational activities are in line with the objectives of the organization.
- (ii) To assure management that MIS has been functioning properly to attain organizational objectives.
- (iii) To assure management that the management control system is functioning efficiently and effectively.

The operational audit is more of a technical analysis for appraisal and review rather than a financial cum accounting analysis under financial audit. In Operational Audit the audit functioning and objectives reach out beyond the financial control aspect into the operating areas of the business.

Difference Between Financial Audit and Operational Audit

A clear cut difference between financial audit and operational audit can't be drawn in many cases. Both are not mutually exclusive. They are interconnected and interlinked. However, difference between the two may be stated as under :-

Financial Audit

- (a) To see that established systems and procedure are complied with.



- (b) To see that proper records have been maintained for the fixed assets of the concern.
- (c) To look into the correctness of financial data and records alongwith correctness of the accounting procedure/standards followed.
- (d) To see whether scrap, salvage and surplus materials have been properly accounted for etc.
- (e) To see the Internal Control System has been working properly.
- (f) To see that any abrupt variation in sales, purchases etc. with respect to immediate previous year are not due to any irregularity.
- (g) To see that the credit control has been strictly followed.
- (h) To see that all payments have been made with proper authorization and approval.
 - (i) To see that preparation of salary and wage payroll has been properly done.
 - (j) To see that all statutory obligations have been complied with.

Operational Audit

- (a) To examine whether the accounting operational functions have been true with the management objectives.
- (b) To see that Internal control system has been working properly.
- (c) To see that the financial accounting records have been properly designed and maintained to furnish management with timely information to help them of judging to what extent the profitability goals have been achieved.
- (d) To study whether scrap/loss of materials have remained within the permitted limits.
- (e) To see the Internal Control System has been working properly.
- (f) To study the reasons for unfavourable variances.
- (g) To study the credit control system for suggesting better means where considered necessary.
- (h) To study whether the expenditure has remained within budgetary provisions.
- (i) To see that the payments are well within budgeted amounts and there is proper utilization of manpower.

The operational audit is more of a technical analysis for appraisal and review rather than financial analysis. In Operational Audit, the audit functioning and objective match out beyond the financial control aspect into the operating areas of business.

Concept of Efficiency Audit

The term efficiency audit means studying competence to achieving goals. The objective of efficiency audit is to ensure that management controls are functioning effectively and efficiently in every functional or operational areas of business.

The appraisal and review under efficiency audit be divided into following two segments :-

- (a) Adequacy of qualities and qualification of the personnel working to attain business objective.
- (b) Effectiveness of the tools and techniques applied in achieving the objectives.

Audit appraisal under efficiency audit includes the following :

- (i) Reduce the areas of uncertainty in business.
- (ii) Remove the bottlenecks to achieve the goals and objectives of the organization
- (iii) Safeguard against the causes of business failures.
- (iv) Remove the inefficiencies and ineffectiveness of operations resulting in cash drainage or other losses.
- (v) Strengthen the factors for survival and prosperity of the business. The internal audit, under efficiency audit, is to find out whether :-
 - (a) Any delay in decision making has led to additional financial costs.
 - (b) Any operation of managerial process has led to ineffective or delayed operation of a project.
 - (c) The area of operation has been managed in an economical and efficient manner in terms of appropriate utilization of man power, plant and machinery, finance, time and material.
 - (d) Inefficiency has led to non-achievement of targeted production and productivity.



The efficiency and the effectiveness of an executive in discharging his obligation towards the attainment of organizational objectives and goals will also form part of efficiency audit.

Propriety Audit

Kohler has defined propriety as “that which meets the test of public interest, commonly accepted customs and standard of conduct and particularly as applied to professional performance, requirements of Govt. regulations and professional codes”.

Propriety Audit would mean whether the transactions have been done in conformity with established rules, principles and some established standard. The Propriety Audit would mean the verification of following main aspects to find out whether :-

- (i) Proper recording has been done in appropriate books of accounts.
- (ii) The assets have not been misused and have been properly safeguarded.
- (iii) The business funds have been utilized properly.
- (iv) The concern is yielding the expected results.

The system of Propriety Audit is applied in respect to Government Companies, Government Department because public money and public interest are therein involved.

It is an essential function of Audit to bring to light not only cases of clear irregularity but also every matter which in its judgement appears to involve improper expenditure or waste of public money or stores, even though the accounts themselves may be insufficient to see that sundry rules or orders of competent authority have been observed. It is of equal importance to ensure that the broad principles of orthodox finance are borne in mind not only by disbursing officers but also by sanctioning authorities.

Voucher Audit

“Voucher is a piece of paper or a written document which confirms the truth of anything. As for example, a receipt obtained from the payee after disbursement is a voucher.”

Any audit with reference to some documentary evidence may be termed as voucher audit. The financial Audit is mainly carried out with reference to voucher.

Statutory Audit certifies the Statement of Accounts including the Balance Sheet after carrying out audit which is mainly with reference to documentary evidence. However, it should be remembered that after promulgation of the Manufacturing and Other Companies (Auditor's Report) Order 1988, a Statutory Auditor has also to carry out some audit which is not directly based on documentary evidences.

Compliance Audit

It is common to us that the business undertakings require some certified statement on various matters and the auditors certify such statements after carrying out audit which might be necessary under the particular cases. All such audits are called Compliance Audit. Suppose when a company applies to a bank for some loan, a certified statement showing the turnover of the company for the past two or three years along with the current year might be necessary, and for this purpose the certified statements are to be attached with the application, otherwise the application will be rejected. So these certified statements showing the turnover of the company fall under the category of compliance audit. Internal audit for compliance could be more broad base to include compliance which documented procedures / policies, compliance with statutory requirements in the relevant areas etc.

Pre and Post Audit

When payments are made by the business or non-business entities, proper scrutinisation should be made before making such payment. This is known as Pre-audit.

For e.g. when certain payments are made by the business undertakings such as salary, medical bills, traveling expenses etc, these payments should be disbursed after making proper scrutiny by the employees of the concern who are not normally the internal auditor.

But there are some payments, which are to be disbursed within a very short period, and within that time proper scrutiny could not be undertaken by the employees of the concern. Such as, when incentive payments have to be made by a large undertaking to its employees within a day or two then the bill is generally prepared and paid



immediately without carrying out any major scrutiny by the employees of the concern. So after making payment the verification can be made. This is known as Post Audit.

Auditing in depth

In view of large number of transactions of an organisation, it becomes practically difficult for an auditor to undertake detailed vouching and post audit of the large volume. He can conduct a more effective audit, if he concentrates on intelligently selected areas. In such a situation Auditing in depth comes in handy. This means the tracing of a transaction through its various stages from origin to conclusion, examining the supporting records at each stage and ascertaining whether all the requirements laid down in the system of internal check have been complied with e.g. purchase of an item from indent stage to receipt/issue of material, verifying all related activities.

8.2 C A R O – COMPANIES (AUDITOR'S REPORT) ORDER, 2003

The earlier order MAOCARO – Manufacturing and Other companies (Auditor's Report) order 1988, superseded by the new order C A R O – COMPANIES (AUDITOR'S REPORT) ORDER, 2003 issued by the Central Government as per the power granted under section 227(4A) of the Companies Act, 1956 is applicable to an auditor report submitted after 31st December 2003.

According to 227(1A), the auditor is required to report on certain matters only if he is not satisfied after his examination of the accounts but after this new order, the auditor has to make a statement on each of the specified matters likewise in case of Govt. companies, this order is in addition to the directions of the Comptroller and Auditor General in India.

This new order is applicable to every company except,

1. A Banking Company
2. An Insurance company
3. A company licensed to operation as per the provision of Section 25 of the Companies Act.
4. A private limited company which has a paid up capital and reserves of not more than ` 50 Lakhs. If the paid up capital of any company is more than ` 50 Lakhs but having accumulated loss double than the paid up capital or paid up capital and reserves are more than ` 50 Lakhs but the miscellaneous expenditure to be written off are to the tune that if written off paid up capital and reserve balance together will go below ` 50 lakhs, then this order is applicable.
5. Private Ltd. Company whose turnover does not exceed ` 5 crores.

The order is applicable to foreign Companies incorporated outside India but having a place of business within India. The branches of the Companies liable to this order also come under the purview of this order.

The following matters are required to be dealt in the Auditor's Report :-

1. **Fixed Assets** : Auditor should comment whether the company is maintaining proper records of fixed assets, the management verified the fixed assets frequently and the material discrepancies found accounted properly, the substantial dispose of fixed assets has affected considerably the going concern.
2. **Inventory** : The auditor has to make following statements on verification and valuation of inventories.
 - (a) Whether physical verification of Inventory has been conducted at reasonable intervals by the management.
 - (b) Are the procedures of physical verification of inventories followed by the management reasonable and adequate in relation to the size of the company and the nature of its business ? If not, the inadequacies in such procedures should be reported.
 - (c) Whether the company is maintaining proper records of inventory and whether any material discrepancies have been noted on physical verification and if so, whether the same have been properly dealt with in the books of account.



- 3. Loans :** In the case of loans revised, organized to firms etc. covered in the register maintained under Section 301 of the Companies Act, auditor has to make comments on the following :-
- Has the company either granted or taken any loans, secured or unsecured to/from companies, firms or other parties covered under the register maintained under Section 301 of the Companies Act. If so, give the number of parties and amount involved in the transactions.
 - Whether the rate of interest and other terms and conditions of loans given or taken by the company, secured or unsecured are prima facie prejudicial to the interest of the company.
 - Whether the payment of the principal amount and interest are also regular.
 - If over payment is more than one Lakh, whether reasonable steps have been taken by the company for recovery/payment of the principal and interest.
- 4. Internal Control on Purchases of Assets and Sale of goods :** Is there an adequate internal control procedure commensurate with the size of the company and the nature of its business for the purchase of inventory and Fixed Assets, and the sale of goods? Whether there is a continuing failure to correct major weaknesses in internal control?
- 5. Transactions in which Directors are interested :** Auditors statements are required on the following :-
- Whether transactions that need to be entered into register in pursuance of Section 301 of the Companies Act, have been so entered.
 - Whether each of these transactions have been made at prices which are reasonable having regard to the prevailing market prices at the relevant time.
- These should be commented only in the cases of transactions exceeding the value of ` 5 lakhs.
- 6. Public Deposits :** In case the company has accepted deposits from the public whether the directions issued by the Reserve Bank of India and the provisions of Sections 58 A and 58 AA of the Companies Act and the rules framed there under where applicable, have been complied with, if not, the nature of contraventions should be stated; if an order has been passed by Company Law Board, whether the same has been complied with or not.
- 7. Internal Audit System in certain companies :** In the case of listed companies and other companies having a paid up share capital and reserves exceeding ` 50 lakhs as at the commencement of the financial year concerned, or having an average annual turnover exceeding ` 5 crore for a period of three consecutive financial years immediately preceding the financial year concerned, whether the company has an internal audit system commensurate with its size and nature of its business.
- 8. Maintenance of Cost Records :** Where Maintenance of Cost Records has been prescribed by the Central Government under Section 209(1)(a) of the Companies Act whether such accounts and records have been made and maintained.
- 9. Deposit of Statutory Dues :** The Company Auditor has to report that –
- Is the company regular in depositing undisputed statutory dues including Provident Fund, Employees State Insurance, Income Tax, Sales Tax, Wealth Tax, Custom Duty, Excise Duty, Cess and any other statutory dues with the appropriate authorities and if not, the extent of arrears of outstanding statutory dues as at the last date of the financial year concerned for a period of more than six months from the date they seem payable, shall be indicated by the auditor.
 - In case dues of Income Tax, Sales Tax, Wealth Tax, Custom Duty, Excise Duty, Cess have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending may be mentioned, but he should, while reporting, remember that a mere representation to the department should not constitute a dispute.
- 10. Sickness :** Where in case of a company which has been registered for a period not less than 5 years, its accumulated losses at the end of the financial year not less than 50% of its net worth and whether it has incurred cash losses in such financial year and in the financial year immediately proceeding such financial year also.



- 11. Default in Repayment of Dues :** Whether the company has defaulted in repayment of dues to a financial institution or bank or debenture holders? If yes, the period and amount of default to be reported.
- 12. Documents and Records for Secured Loans :** Whether adequate documents and records are maintained in cases where the company has granted loans and advances on the basis of security by way of pledge of shares, debentures and other securities. If not the deficiencies to be pointed out.
- 13. Compliance with Special Provisions :** Whether the provisions of any special statute applicable to chit fund have been complied with, in respect of nidhi, mutual benefit fund or societies –
 - (a) Whether the net owned fund to deposit liability ratio is more than 1 : 20 as on the date of Balance Sheet.
 - (b) Whether the company has complied with the prudential norms on income recognition and provisioning against sub-standard, doubtful or lost assets.
 - (c) Whether the company has adequate procedures for appraisal of credit proposals/requests, assessment of credit needs and repayment capacity of the borrower.
 - (d) Whether the repayment schedule of various loans granted by the nidhi is based on the payment capacity of the borrower and would be conducive to recovery of the loan amount.
- 14. Records of Dealing in Securities :** If the company is dealing or trading in shares, securities, debentures and other investments, whether proper records have been maintained of the transactions and contracts and whether timely entries have been made there in, also, whether the shares, securities, debentures and other investments have been held by the company in its own name, except to the extent of the exemption if any, granted under section 49 of the Companies Act.
- 15. Guarantees for loan taken by others :** Whether the company has given any guarantee for loans taken by other from bank, or financial institutions, the terms and conditions where of are prejudicial to the interest of the company.
- 16. Application of Term Loans :** Whether the term loans were applied for the purpose for which the loans are obtained.
- 17. Financial Management :** Whether the funds raised on short term basis have been used for long term investment and vice-versa, if yes, the nature and amount is to be indicated.
- 18. Preferential Allotment of Shares :** Whether the company has made any preferential allotment of shares to parties and companies covered in the Register maintained under Section 301 of the Companies Act and if so whether the price at which shares have been issued is prejudicial to the interest of the company.
- 19. Creation of Security in Respect of Debentures :** Whether the securities have been created in respect of debentures issued.
- 20. Disclosure of End-use of money raised from Public issue :** Whether the management has disclosed on the end use of money raised by public issue and the same has been verified.
- 21. Fraud :** Whether any fraud on or by the company, has been noticed or reported during the year, if yes, the nature and the amount involved is to be indicated.

The order stipulates that if the auditor given negative qualified answer to any of the above questions on which a statement is required on his report, he should give the reasons for that and where he is unable to give any opinion he should indicate this fact with reasons. The unfavourable answers to any of the question does not mean that the opinion of auditor on the true and fairness qualified answer the auditor can give an unqualified audit report, if the qualified answer does not materially affect the financial position discussed in the Profit and Loss Account and for Balance Sheet. The Board of Directors is supposed to give comments, in its annual report, on the adverse statements made by the auditor under the order. In short, the order provides a different orientation to a company audit. Unlike traditional auditing, due to the provisional Section 227(1A), the auditor was required to offer his comments as an expert on certain transactions of the company and to enquire



whether certain transactions were prejudicial to the interest of the company. The order under Section 227(4A), extend the scope of audit even further e.g. Auditor has to comment on the internal audit system, internal audit system, records of fixed assets etc.

8.3 INTERNAL AUDITING FUNCTION

It is an accepted fact that internal auditing function to be effective, must be independent of the activities to be audited. For this, Internal Audit Department must have some accepted standing in the organization. But it cannot be a fully independent department for obvious reasons. Total independence would be as elusive as a perfect vacuum. Complete independence would imply freedom from all types of dependency including financial dependency. Hence as long as Internal Audit Department would remain a part of the organization and receives its life blood from the enterprise, it must forgo some independence. A compromising situation is, therefore, desirable. The department must have the greatest amount of practical independence in the real world situation to protect it from having to compromise with audit objectives. The necessity of the practical independence is being recognized more and more by the modern business concerns and the percentage of firms where the auditing organization reporting to vice-president/the board is on the increase. A very convenient agreement would be auditing organization answerable to an officer whose own status would be sufficiently high to enable him to consider the internal audit report and taken action on the audit recommendations. Preferably such officer should be a member of a Board's Auditing Committee.

The role of internal auditor is in the process of being properly recognized. The growing size, technological advancement and the complexities in running an organization has made it imperative on the part of the progressive management to recognize and utilize the services of the internal auditor as a tool of management control. Many of the constraints and bottlenecks in proper management of business can be overcome through the constant appraisal and review of the operations with the help of the internal auditor.

The auditor's role should be defined in the written document to be approved by the management and the Board of Directors. Such a documentation should include, *inter alia*, the following vital aspects :-

- (a) Organisational status and position to be indicated in the organization chart.
- (b) Defining the scope of internal audit operations.
- (c) Authorise the internal audit department to have access to all records, personnel and properties.
- (d) A declaration to be known to all personnel in the organization at all levels, for their cooperation and coordination for all activities of internal audit operation.

At times there is an uneasy feeling that the internal auditor is an interloper, reporting to management of the inefficiencies or deficiencies of the departments audited by him. The internal auditor a helping tool to management in prompting efficiency and cost reduction and hence, if he cannot drive away the resentment and/or criticism of others, the purpose of audit may get frustrated. In fact the internal auditor has to get cooperation from employees of other departments, who have to sincerely believe in his honesty of purpose. The internal auditor should be placed in such a status in the organizational set up so that he can be an effective instrument of management control process.

We often remark, the tree is known by the fruits it yields. Internal audit department by virtue of its important position, have access to all books and records. If like a professional doctor, the department can ascertain the ill health of the organization related through various area of inefficiency and can suggest medicine-like tips in the form of recommendations, which give positive result, the status of the department is bound to go high, and the CIA would definitely occupy a key position in the management team.

The chief of internal auditor should submit annually to management for approval and to the Board for its information a summary of the department's audit work schedule, staffing plan, and financial budget. He should also submit all significant interim changes for approval and information.

The chief of internal auditing should submit activity reports to management and to the Board annually or more frequently and recommendations and should inform management and the Board of any significant deviations from approved audit work schedules, staffing plans and financial budgets, and the reasons for them.



Auditing The Functions of An Enterprise

Pay Roll – Salary and Wages Administration

The basic documents that would be examined in this connection would be as follows :-

1. Appointment letter—authority to appoint.
2. Service rules, has pay scales.
3. Circulars issued by the Government and the management
4. Attendance records
5. Employees history cards
6. Accounting manual
7. Payment vouchers—statutory and other deductions.
8. Statutory laws and rules etc.

The following may be stated to be the objectives of Internal Auditing in this area :-

1. Accuracy of pay roll
2. Effectiveness of Internal Control System
3. The functioning of the management information system
4. Accuracy and adequacy of documentation
5. Observance of statutory laws and rules.
6. Accuracy of the financial and cost accounting system

The audit steps that would be taken as under :-

- (a) Check the records, appointment letters, personal files etc. for examining authorization for employment and rates of pay dearness and other allowances should also be checked as to whether revision in rates of pay or increments are properly authroised. In case the dearness allowance is based on cost of living index, examine whether such DA has been calculated correctly.
- (b) Check whether deductions from pay roll are properly authorized
- (c) Check the correctness in recording attendance and time shown as spent on jobs whether some production bonus etc. might have been billed for.
- (d) Examine the accuracy of records starting with engagement of workers and ending with disbursements of salaries etc.
- (e) Examine whether the employment, rates of pay, promotions and increment are in agreement with the policy declared by the company.
- (f) Check the clock-cards with the total number of workers on the pay roll.
- (g) Check the hours shown in the clock-cards with the hours as per timecards or job cards.
- (h) As a test-check, physically verify the number of workers when they are at work in a department and see whether the same tallies with the pay roll and the employments records.
- (i) In case there is an incentive scheme, examine the procedure and control thereof. Check the incentive payments with production/sales figures.
- (j) Examine the leave records and see whether the leave has been duly sanctioned.
- (k) Examine the authority and responsibility in sanctioning overtime, study whether the overtime payment is justified. Examine whether overtime has been properly accounted for. See, whether the overtime expenditure has remained within the budget provision.
- (l) See, whether there is compliance with the provisions of the statutory laws and rules like Factory's Act, Minimum Wages Act, Industrial Disputes Act, Payment of Wages Act, Payment of Bonus Act, Workmen's Compensation Act etc.
- (m) Is the payroll prepared well in time? Is their proper coordination between the accounts department, pay roll section, personnel section and production department ?



- (n) Check whether proper record is kept with regard to unpaid wages. See whether the subsequent payments are properly controlled and accounted for.
- (o) Find out the reasons for significant variation between actual cost and budgeted cost.
- (p) Examine the procedure for termination of employment either by resignation, discharge, retirement etc. See whether the names of such employees are eliminated from the records to avoid their inclusion in the pay roll, examine also the final settlement made in such cases.
- (q) Study (if desired by management) the extent of mechanization of accounting possible, in case of pay roll. In case there is the existence of mechanization, study its correctness. The Internal Audit may also conduct "O & M" study if so desired by the management provided it is equipped for the purpose. The study may include the improvement of the following by changing work flow, mechanization etc. Pay roll form, recording by production department, time-office etc., collection of data for management from primary records etc.

(A) Fixed Capital Assets

Basic document for review would be as under :-

- (i) Authorisation for acquisition and sale
- (ii) Purchase order/contracts
- (iii) Policies on depreciation, amortization
- (iv) Asset Register
- (v) Account Manual/Plant Operation Manual.

The objective of internal auditing would be :-

- (i) Effective utilization of assets.
- (ii) Make or buy decisions from the point of view of economy
- (iii) Adequacy of security and safety measures
- (iv) Compliance with Accounting/Plant Operation Manual. Manufacturing and Other Companies (Auditor's Report) Order, 1988 guidelines issued by the professional accounting bodies etc.
- (v) Adequacy of insurance coverage
- (vi) Correctness of fixed assets schedule - Verification of assets
- (vii) Verification of Payments and accounting—verification of assets.
- (viii) Verification as to the correctness of the depreciation schedule and its accounting etc.

The audit steps would be as under :-

(B) Authorisation

- (a) Examine the procedure of capital expenditure authorization.
- (b) Does the cash flow statements reflect the amount as authorized for capital expenditure so that fund is available at the appropriate time ?
- (c) Whether the actual expenditure has exceeded amounts authorized? If so whether the additional expenditure has been authorized subsequently?
- (d) In case, there is expenditure for some additional facilities to increase production, examine the result achieved with reference to actual production and sale.
- (e) Verify the purchase order of acquisition of capital assets. See, whether the purchase orders include protective clause like guarantee/warranty, keeping of retention money etc.
- (f) Examine the credit contract and see whether the terms and conditions thereof have been duly complied with.
- (g) Assess the productivity and profitability of fixed capital expenditure.
- (i) Examine whether the title deeds to the properties like land, building etc are in order.
- (j) Examine whether distinction is made as between capital expenditure and revenue expenditure.



- (k) In case some assets have been acquired through hire-purchase scheme, review the terms and conditions of hire purchasing agreement and examine the accounting aspects of capitalization in that light.
- (l) In case there is some make or buy decision, examine the results on the basis of the actual.

(C) Depreciation

- (a) Examine the policy of the company for charging of depreciation.
- (b) Examine whether the method of depreciation and the rates of depreciation are reasonable and sound considering the nature of assets, its operation and estimated life.
- (c) Examine whether the rates of depreciation applied and the assets classification are correct according to accounting manual, in case such manual exists.
- (d) Examine the depreciation schedule prepared for annual accounts to see whether depreciation for all the existing assets in operation has been included. Also see whether advantage has been taken of the provisions of Income Tax Act and Rules to get maximum depreciation allowable.
- (e) Review the compliance of Schedule VI of the Companies Act 1956. Compliance of Section 205 Payment of dividend out of profit only and Section 350 (Ascertainment of depreciation) of the Companies Act 1956.

(D) Physical Verification

- (a) Examine whether there is any system of physical verification of assets at regular intervals.
- (b) Examine and compare the equipment history cards as maintained by the Engineering Department with the assets register as maintained by the Accounts Department
- (c) Obtain a list of the obsolete/discarded assets and see whether the assets declared obsolete or discarded have been deleted from the Asset Register. See whether these assets have been disposed off promptly at the best price.

(E) Retirements

- (a) Examine the procedure of retirement of assets and the authority and responsibility of persons connected therewith.
- (b) Has any asset been transferred to another location, has any asset been discarded even though its life has not expired ? If so, study the reasons thereof.
- (c) In case of sale of any asset, examine whether the sale has fetched the best price and been done under proper authority.
- (d) See whether proper records are maintained in respect of assets discarded.
- (e) See whether accounts adjustments have been carried out in respect of discarded assets.
- (f) See whether the accounts department get timely information regarding assets discarded.
- (g) See whether assets retired during the year tally with the Assets Schedule prepared for the year of accounting and taxation purposes etc.

(F) Idle Facilities

- (a) Find out the reasons for idle facilities.
- (b) Review the plans, procedure for control of idle facilities.
- (c) Examine the scope for utilization of the idle facilities. Can the facility be leased out?
- (d) See whether any review report is made periodically for facilities remaining idle etc.

General Points

- (a) Examine the insurance policy covering the risk against fire, storm, riot etc.
- (b) Ascertain the reasons for non-insurance of some assets, if any.
- (c) Examine whether there is proper scheme for carrying out preventive maintenance.
- (d) Examine whether there is any procedure for periodical assessment of the productivity of the assets in operation.
- (e) Study whether installation of assets/additional facilities are based on projection report etc.



Audit of Receivables :

Where the maximum business of the undertaking is the sale of goods or products on credit, the balances due from the customers at the Balance Sheet date would be presented by the debit balances in the Sales A/C on that date. This would generally be the most important of receivables.

The audit of the balances would comprise :-

- (a) An examination of the system of internal check for regulating the sale of goods, the receipt of remittances from the debtors, the granting of discount, the writing of bad debts etc.
- (b) Vouching to establish the accuracy of the entries recorded in the sales ledger.
- (c) Testing to establish the arithmetical accuracy of the balance shown by the sales ledger.
- (d) Study of the age and other factors to assess the possibility of bad or doubtful debts.

Sometimes, credit balance might be noticed in some individual debtors accounts. This should be scrutinized with care because their existence may signify the omission of debit postings. If their authenticity is established, the auditor should see that they are grouped with the current liability and not deducted from the total trade debtors.

The audit of sales ledger should be linked with the audit of stock of finished goods with a view to preventing or detecting :-

- (a) Duplication of inclusion against sale of some goods
- (b) Omission of posting of some sale.

Such errors are common where goods are invoiced in advance of delivery or there is some delay in invoicing following deliveries from the stock as gross profit is affected by such transactions—efforts should be made to relate the sales to the correct period and then to make adjustment of inventories to avoid duplication or omission.

The internal audit may also consider whether there has been any window dressing by accelerating deliveries to the customers during the closing days of the financial year.

The internal auditor must also see that the sales ledger does not include any sales not occurring under the ordinary course of business. As for example sale of fixed assets should not be included in the sales ledger.

Verification of balances arising from sale of by-products, scrap etc. would depend to a large extent on the efficiency of Internal Check for controlling such transaction. It should be noted that Sundry Sales is an area where defalcation is common.

The internal auditor therefore, should see that such transactions have passed through a requisite internal control system.

Audit of Inventory

Purchases – See whether there is a purchase manual. The Internal Auditor should then, jot down the important factors that has been prescribed in respect of purchase of raw materials etc.

Normally purchases are based on five important factors given below :-

- (1) Right Price.
- (2) Right quantity
- (3) Right quality
- (4) Right delivery and
- (5) Right supplier

The auditor therefore, has to see that these principles have been duly followed. Based on the above principles the audit steps would be generally as follows :-

Inventory Control

Receiving :

- (i) Examine the systems and procedures of receiving, checking and recording of stores, materials and the authority and responsibility of the persons involved in the process.



- (ii) Examine the procedure of inspection of materials – see whether there is proper coordination between the Inspection Department and the Receiving Section of the Stores Department.
- (iii) Examine the procedure of preparing Material Report – How many copies of the report are prepared? To whom these are endorsed? Are all necessary? What is the time lag between receipt of material and its inspection?
- (iv) Has any demurrage been paid to the railways for late clearance of materials?
- (v) What is the procedure of receipt of materials returned from the Production Department?

Keeping of Stock :-

- (i) See whether the physical condition of the stores in stock is periodically verified.
- (ii) Study the arrangement to facilitate receiving, storing and issue of stores
- (iii) Study whether heavy materials / materials for immediate consumption are delivered directly to the work - sites.
- (iv) Study the arrangements and precautions taken in respect to hazardous handling, safety measures to prevent theft, fire, deterioration etc.
- (v) See whether any sub-stores / site-stores exists.
- (vi) See whether facilities exist in storing materials in well-arranged bins etc.

Procedure of issue and recording :-

- (i) Examine the procedure of issue and records maintained in the stores section.
- (ii) What is the time lag between placing the issue requisition and actual issue to the consuming department?
- (iii) Review the frequency of issues to the consuming departments. Is it possible to reduce the frequency?
- (iv) Has there been issue without properly authorized requisition? If so, ascertain the reasons thereof.
- (v) Does the person drawing the material signs the issue voucher? Similarly does the assistant issuing the materials from stores similarly sign the issue voucher? Examine the authority and responsibility of the persons involved in the process.
- (vi) Review the issue procedure and documentation in respect to issue to contractor engaged in construction/ maintenance jobs.
- (vii) Did the production suffer due to non availability of materials from stores? Ascertain the reasons therefor.
- (viii) Has there been any sale of stores materials to employees? If such system exists, review the systems and procedures in issues, recording, accounting and realization of money from the employees.
- (ix) Examine the procedure and documentation in respect to materials returned. Is any Stores Return Note issued for the purpose? Are the information adequate for the purpose of accounting and receipt of materials in the stores?
- (x) Review the procedure of recording and return of empty containers.
- (xi) In case a stores manual exists, see, whether instructions contained therein have been followed in issuing the materials and their documentation etc.

Physical Verification:-

- (i) Review the procedure of physical verification of stores? Is it done in the year end? Or the physical verification is done on perpetual inventory system basis.
- (ii) If a system of perpetual inventory exists, see whether the stores are covered at least once in a year and important stores are covered more than once.
- (iii) Does an independent stock verification wing carry out physical verification of stores?
- (iv) What records are prepared in respect to recording of stores found short / surplus?
- (v) What is the procedure in making adjustment of stores records / financial records on the basis of shortage / surplus report ?



- (vi) Under whose authority this discrepancy report is issued.
- (vii) To whom physical verification department reports ?

Stores Accounting :-

- (i) Is there any Stores- Accounting Manual duly approved by the management ?
- (ii) Who maintains the stores ledger ? If maintained by the stores people in addition to bin cards, is it periodically reviewed and reconciled with accounts by some accountants working in the Accountants' Offices?
- (iii) Examine whether accounting/recording of stores received/stores returned from production department, stores issued for consumption has been done as per procedure of the Stores Manual.
- (iv) See whether the stores ledger/bin cards contain all the required information like unit price, maximum, minimum, reorder, economic order quantity etc.
- (v) Examine whether the system of receiving / issuing of stores etc. ensure that only the authorized transactions are recorded.

Inventory Control and Management :-

- (i) Has the inventory been classified for proper control ? Is A, B, C system of inventory classification followed?
- (ii) How the inventory levels – maximum, minimum, reorder, economic order quantity fixed?
- (iii) Is material budget prepared in advance to regulate purchase ?
- (iv) Study the opening/closing stocks of the last few years.
- (v) Study the procurement of materials for the last 2/3 years and see whether the same compares favourably with production.
- (vi) Is there any regular system to assess slow-moving/non-moving stores items for early disposal in cases considered necessary ?
- (vii) Who is the person to declare some material as surplus ? Who authorizes its disposal?
- (viii) Review whether value analysis, PERT etc. are applied for better management of stores.
- (ix) Work out inventory ratios to judge the reasonableness of inventory build up
 - (a) Working Capital to Store Inventory
 - (b) Current Assets to Store Inventory
 - (c) Inventory Turnover.

Some General Aspects :-

- (i) Sometimes used materials are returned to stores. In such cases procedure for recording would be the same as followed in case of unused materials except that these may or may not be priced. Usually separate stores ledger / bin cards are opened. See whether the procedure in this regard has been observed.
- (ii) Review whether any study has been made in regard to mechanization in stores receipt/issue, store accounting.
- (iii) Review whether proper numerical accounts have been kept in respect to stand by spares.
- (iv) See whether there are any Material Receiving Report pending disposal – recording valuation in stores ledger/bin card, accounting the accounts records etc.
- (v) Review the mode of valuation of closing stock.
- (vi) How soon the stores schedule is prepared for annual accounts purpose ?
- (vii) Are the stores materials adequately covered by insurance against loss from fire and other risks ?
- (viii) Is there proper coordination between –
 - (a) Central Purchase Department



- (b) Local Purchase Department
- (c) Stores Department
- (d) Stock – verification Department
- (ix) In case there are number of factories producing same / similar products make comparative study regarding –
 - (a) Surplus materials
 - (b) Obsolete/slow-moving materials.
 - (c) Finished/work-in-progress stock
 - (d) Opening/closing stock of raw material, etc.

Apart from the above, O and M study may be carried out for standardization of forms, modification of work flow for improvement in efficiency in various directions etc.

Production Planning and Control

The objectives of Internal Audit in this area would be to see whether :-

- (i) Records maintained are adequate and reliable.
- (ii) Production planning and control is effective.
- (iii) Management reporting system is adequate.
- (iv) Utilization of facilities has been done efficiently.
- (v) Financial and cost accounting including reconciliation between production, work-in progress, sales and inventories have been done correctly.

Keeping in view the above, the different audit steps would be as under :-

- (i) Review the nature of the business, its operation, plans policies and objectives of the management which would be a guide for appraisal and review of the adequacy of production planning and control techniques.
- (ii) Study whether any inter-firm and intra-firm comparison is made to assess efficiency in production and productivity.
- (iii) Is there any industrial engineering department to look after plant performance, utilization of man, machine and material.
- (iv) Examine whether proper coordination exist between the following departments.
 - (a) Production Planning Department.
 - (b) Industrial Engineering Department.
 - (c) Material Management Department.
 - (d) Commercial or Accounts Department
- (v) Examine whether a sale forecasting is made in advance to control production.
- (vi) Study the actual production with the requirement as per sales forecast. Study whether the time schedule has been maintained in achieving the actual production.
- (vii) Review the existing production planning, scheduling and control system, examine whether production planning and scheduling have been applied to production process efficiently.
- (viii) Examine whether the production planning and control are within existing facilities.
- (ix) Examine whether any production control flow chart is in operation. Such flow chart would show the sequence and scheduling of production process from receipt of the order to dispatch of the finished goods.
- (x) Examine the actuals with reference to the production flow chart and suggest improvement to the flow chart based on the actual study. Study production scheduling, inventory control, extent of machine and labour utilization from the point of view of control of production.
- (xi) Review whether delivery schedules as given in the sales order have been complied with. Analyse the reasons for non delivery according to delivery schedule. Recommend remedial measures.



- (xii) Has any job been given on subcontract, if so, analyse the reasons thereof. Study whether these could have been done by utilising the existing facilities. Has the subcontractor delivered the goods within the time schedule agreed upon ? Has the goods supplied by the subcontractor been found satisfactory from the point of view of quality, specification and other related matters ?
- (xiii) Does any Inspection Department exist ? If so, review the records of inspection maintained by the inspection department. Study whether the inspection has been done expeditiously. Suggest improvement of the present records when considered necessary.
- (xiv) Examine the file containing complaints from the customers. Examine, whether proper action has been taken on the basis of the complaints lodged. Assess to what extent there has been financial loss for supplying defective goods (production defects). See whether any comprehensive report in this regard is placed to the management. If so, who is responsible for the job ? Has he discharged his responsibility satisfactorily.
- (xv) Review the records in general and recommend simplification/improvement if possible etc.

Marketing

Marketing would include mainly sales, sales accounting and credit controls. The main objectives of internal audit in that area would be as under :-

1. Adequacy and reliability of sales record and accounting
2. Accuracy of Customers A/c.
3. Effectiveness of sales planning and control.
4. Compliance with statutory requirement, payment of Sales Tax, Excise Duty etc.
5. Adequacy and effectiveness of existing management information system and internal control system.

Based on the above, internal audit function in respect to important aspects is being discussed below :-

Sales Order :-

Examine and review :-

- (i) Whether the terms and conditions of sales effected covers all the important aspects like terms of payment, delivery charge, discount for payment within the time schedule etc.
- (ii) The procedure of issue of sales order.
- (iii) Whether sales orders are booked on the basis of written requests.
- (iv) The time lag between receiving the customers' letters and issue of sales order and actual dispatch of goods. Is the time lag reasonable ?
- (v) At what point the customer is allowed to cancel an order ?
- (vi) Whether any customer's request is still pending ?
- (vii) Whether any customer's order is rejected ? Ascertain the reasons.
- (viii) The authority and responsibility of signing the sales orders. Whether different officials have been authorized for signing sales orders of different amounts ? If so, the limitations imposed have been properly adhered to by the officials authorized for the purpose.
- (ix) Whether any revision of the sale prices are promptly notified and acted upon etc.

Despatch :-

Examine and review :-

- (i) The systems and procedures of despatch and the records maintained for the purpose.
- (ii) The despatch dates with the dates given in the despatch schedule and sales orders.
- (iii) When the despatch documents with invoices are sent to the customers after despatch of goods ? Is the delay unusual ? If so, suggest remedial measures. Whether there is any complaint from any customer on account of receipt of despatch documents after arrival of the goods. (This might mean that the customer might have been required to pay demurrage charge).
- (iv) Authority and responsibility for signing despatch documents etc.

**Sales Invoice :-**

- (i) Review the systems and procedures of invoicing; who prepares the invoices. Is there any second person to check it ?
- (ii) Review the time lag between despatch, invoicing and mailing the same to customers.
- (iii) Check the invoices (test check) with reference to price list, agreement with customers, and other terms and conditions of sales.
- (iv) Check whether trade discounts, cash discount and rebates are allowed as per allowed price list, terms of agreement etc.
- (v) Examine whether Sales Tax/Vat has been correctly charged both in cash memos and credit sales invoices.
- (vi) Ensure that for all goods despatched, sales invoice have been raised. Review the internal control system in operation in this regard and suggest change if considered necessary.
- (vii) Do the invoices show terms of payment and due date of payment?

Credit Control :-

- (i) Examine the procedure of determining of credit worthiness of the customers. Is there any system of reassessing the credit worthiness of the customers ?
- (ii) Examine and review the factors taken into consideration in the following cases :
 - (a) Cash against delivery.
 - (b) Limitations of credit as to payment and amount
 - (c) Documents through bank (payable on presentation of letters of credit, against draft etc)
 - (d) Collection of cash/cheque by salesman.
- (iii) Is there any procedure of reviewing the debtors ledger periodically ? Is any Debtors' List prepared according to Age ? Is there any procedure of charging interest for delayed payment ? It is often noticed that sales terms include payment clause authorizing charging of interest for delayed payment. But usually this is not acted upon. In such cases some report is sent to the management to ensure early payment by them etc.

Debtors Ledger :-

- (i) Examine whether the debtors ledger is kept up-to-date.
- (ii) See whether the debtor's ledger balances are periodically reconciled with the control as in general ledger.
- (iii) Examine whether adjustment entries – debits/credits have been correctly posted (journal entries may be referred to for the purpose)
- (iv) See whether there is a system of confirmation of the balance owing by the customers. Examine whether statutory auditors insist on confirmation of the balances by the debtors.
- (v) Examine the amount written off as bad debts and the amount provided for against doubtful debts. Compare the figure with the same in earlier two-three years. In case the bad and doubtful debts provided for the current years is unduly high, carry out a thorough examination to ascertain the reasons therefor.
- (vi) See whether there is any system of accepting advances or security deposit from the customers. In case such system exists examine the policy followed in this regard. Also see that the advances have been promptly adjusted or the security deposit refunded etc.

Receipt of Cash/Cheque :

- (i) Examine and review the system of receiving cheque/cash. Review the management policy in regard to cash collection. If the policy followed in this regard is one that encourages cash collection, suggest its modification so that cash collection can be avoided to the extent practicable to examine the procedure of issuing receipts after getting cheque/cash against sales. See whether cash collection is against printed receipts. In case of receipts of cheque see whether a provisional receipt is issued which is confirmed after clearance of the cheques received.



Review time-lag between clearance of cheque issuance of pukka receipts.

- (ii) See whether the cash collection is banked at the earliest convenient and the same is not utilized for expenses. If there is no clear management policy in this regard, suggest a policy in the above line etc.

Credit Notes :-

- (i) The credit notes are issued for the following reasons :
- (ii) Examine and review the system and procedure of issuance of credit notes and its recording and accounting.
 - (a) Return of materials
 - (b) Excess/incorrect charges in invoices
 - (c) Cash discount for prompt payment
 - (d) Short delivery/wrong delivery/delivery of defective materials
 - (e) Examine the authority for signing the credit notes
 - (f) See whether the credit notes are promptly issued, documented and accounted for etc.

Debit Notes :

Examine and review whether debit notes are issued in all cases where there has been undercharge in the invoice, recovery of further charges not included in original invoice, delivery of excess material accepted by the customers etc. See also whether debits have been signed by some official authorised for the purpose.

Sales Return :

- (i) Examine and review the procedure adopted in receiving and recording of the sales return.
- (ii) Compare the sales return with total sales. If the amount of sales return is considered high ascertain the reasons therefor and suggest remedial measure.
- (iii) See whether freight charges incurred in returning the sales are borne by the customer for the concern. Examine whether there is clear policy in this regard.

Stock records and accounting:-

- (i) Review the stock card and other records maintained and assess whether they are adequate?
- (ii) Examine the system and procedure of recording entries and accounting.
- (iii) Is stock holding as per sales budget ?
- (iv) Is there any procedure of making age analysis of stocks held ?
- (v) At what intervals stocks are physically verified ?
- (vi) Review whether valuation of stock is being made on some consistent basis etc.

After Sales Service :-

- (i) Examine the policy and procedure followed in respect to after-service.
- (ii) Examine the administrative control to make sure that proper service has been rendered to the customers.

Branches and Depots :-

- (i) Examine the system of administration of sales through depots/branches. Is there any written policy in this regard?
- (ii) What records maintained by the branches/depots?
- (iii) Are the record maintained in respect to entries made for resale? If so, under what circumstances? Has the requirement in this regard been complied with by the branches/depots?
- (iv) Is any cash book maintained for receiving cash/cheque on account of sale and for expenditure authorized to be incurred by the branches/depots? Examine whether such records have been maintained properly?



- (v) What is the procedure of remittance of sale receipts to the Head Quarters by the branches/depots ? Examine whether remittances have been done according to the instructions in this regard.
- (vi) Are the expenditure/income of the branches/depots regulated by budget provision? If so, examine the performance of the branches/depots with reference to the budget provision. In case of significant variation, ascertain the reasons therefor.
- (vii) Are the branches/depots authorized to make sales on credit? If so, review the debtors ledgers and ascertain old debtors.
- (viii) At what intervals, stock at branches/depots are physically verified? Is there any procedure for verification of stock by the staff of the branches/depots? etc.

Research and Development :-

- (i) Examine the organisational structure of the Research and Development Department. Are the research projects undertaken in time with the management objectives?
- (ii) Are the research projects covered by the budget provisions?
- (iii) Are the personnel engaged in the research project duly qualified and experienced ?
- (iv) Examine the completed research projects in the last 2/3 years. How many of them have become successful? What benefits had been derived commercially by the concern out of successful research projects ?
- (v) Is there any procedure of continuous review of the research projects in-progress ? To discontinue those, the possibility of success of which would be found definitely doubtful.
- (vi) How the cost of the research projects accounted for ? Is there any definite management policy in this regard ?
- (vii) What records are maintained by the department in respect to projects undertaken and the cost incurred on them ? Are the records adequate ?
- (viii) Examine whether research and development department has been provided with all necessary facilities for successful research operation.
- (ix) Have proper precautionary measures been adopted to keep the research and development work confidential.
- (x) Review whether Research and Development department has been provided with all necessary facilities for successful research operation.
- (xi) Is there cooperation between Research and Development Department with engineering and other departments?
- (xii) Review the Incentive scheme adopted for motivating the research personnel for carrying out research jobs to the best interest of the organization.
- (xiii) Does the Chairman /Vice Chairman meet periodically with the Head of the Research and Development Department to encourage him in research jobs and to solve the difficulties he might be facing in this connection etc?

Auditing The Internal Auditing Function

Internal audit carries out audit functions to see that the objectives of the management in running the business operations are achieved through realization of some optimum profit. It is a management tool which helps the management in running the business efficiently in accordance with the policies followed at present. Not only that Internal Audit helps to modify the business policies for improvement in efficiency of business operations in future. Actually Internal Audit departments in different business organizations in U.S.A. and other countries have been playing vital role in this regard.

It would, therefore, be apparent that it is necessary to ensure that the Internal Audit Dept. discharges its functions in a desirable manner to be useful as a management tool. It is in this context necessary that an eye is kept on the Internal Audit functions to see whether the same are being done efficiently.

Therefore, audit of Internal Audit functions is considered necessary. However, it should be appreciated that keeping another audit department to carry out such audit does not seem to be a practical proposition.



8.4 PLANNING THE INTERNAL AUDIT PROJECT

The advantages and disadvantages of a standard audit project is a subject of continuous debate amongst Internal Auditors. No planned audit project can be totally applicable without any variation in accounting procedures that are found, in an organization even if there exists a reasonable measure of standardization. However, it has been experienced that in a well established organization where system of internal checks are adequate, the most effective auditing can be conducted by apportionment of audit time approximately 2/3rd. over a Standard Internal Audit Programme adopted to local circumstances and 1/3rd to whose accounting features that appear to auditor the merit of special audit attention.

The advantages of a standard project are as follows :-

1. It provides the internal audit staff, a framework for his activities in logical sequence.
2. It indicates lesser test checking which is necessary on the assumption that the internal check system is adequate.
3. It is of a big help and support to the external auditor who chalks out his own audit programme auditable, avoiding duplication area.
4. It enables a balanced audit to be achieved at each accounting point, also in the entire organization.
5. It also guides the Internal Auditor on the subject of recommendations.

It must be remembered that planning the audit project is mental process but a planned audit project is not a substitute for thinking.

Audit Programme :-

An Audit Programme is a detailed plan of audit assignment to be completed, specifying the methods and procedures to be followed for completing the work of vouching and verification satisfactorily by available staff within stipulated period of time.

Audit Programme is nothing but a plan or programme prepared by auditor for completion of audit specifying the responsibilities of each staff.

In short, before the work of an audit commenced, the auditor should chalkout a programme as to what work is to be done by his assistants and by himself and the time by which the work is to be finished. Audit Programme is a guideline to the internal auditor wherein he wishes out for himself his strategies i.e. how to go about the audit work he is going to perform. The audit programme serves as a guide in developing the appraisal and review techniques suitable to meet the organizational objectives and results expected by the top management. Because of the organizational objectives and results expected by the top management. Because of the usefulness it also serves as permanent comparison to indicate the lines on which management can implement and exercise overall controls.

Developing The Audit Programme

The auditor should prepare a written audit programme, setting for the procedures that are needed to implement the audit plan. The programme may also contain the audit objective for each and should have sufficient understanding to control the proper execution of the work. In preparing the audit programme, the auditor, having an understanding of the accounting system and related internal controls, may wish to rely on certain internal controls in determining the nature, timing and extent of required auditing procedures. The auditor should also consider the timing of the procedures, the coordination of any assistance expected from the client, the availability of assistance, and the involvement of other auditors or experts.

The audit planning ideally commences at the conclusion of the previous year's audit, and along with the related programme, it should be reconsidered for modification as the audit progresses. Such consideration is based on the auditor's review of the internal control, his preliminary evaluation thereof, and the results of his compliance and substantive procedures.



8.5 DETAILED CHECKING VERSUS SAMPLING PLANS

The approach of the auditor would be influenced by the size of the concern he is going to audit. In case of a small or medium sized concern horizontal vouching may give quite satisfactory result. But in big concerns there would be very large number of transactions and hence accounting entries would be huge. It is therefore necessary to have a precise and comprehensive technique in vouching to be applied to a comparatively small sample of transactions without in anyway reducing the effectiveness of the examination. This is actually known as “auditing in depth”. Under it, extremely small sample of transactions of a particular type (i.e. purchase) would be selected and subjected to a critical check in all stages from initiation to conclusion. Stores requisitions, purchase orders invoices, goods receipt notes, prices etc. might be covered under such depth checking technique.

The auditor might continue his examination by reference to entries in the cash book and bank scrolls as regards payment for the purchases. The returned cheques would also be examined. The posting would be checked from the books of prime entry to the ledger. Finally the auditor would examine the stock records which would reflect receipts after issues. This procedure is extremely flexible and may be applied in varying circumstances. If the examination of the successive stages reveals satisfactory results as regards accuracy of recording and the operation of the internal check, the auditor may progressively reduce the number of items to be examined at subsequent stages. This technique virtually leads to the flow chart technique.

Biased Errors :-

These errors arise from bias in selection, estimation etc. For example, if in place of random sampling, deliberate sampling is used in some particular case, there is likelihood of some bias introduced in the result. Such errors are known as biased sampling errors.

Unbiased Errors :-

These errors arise because of a chance errors between the members of population included in the sample and those not included. Thus, the total sampling error comprises of errors due to bias and the random sampling error.

Method of Reducing Sampling Errors :-

The simplest way of increasing the accuracy of a sample is to increase the sample size, i.e. the number of units in the sample.

Flow Chart

A flow chart is a graphic representation of a system. It depicts the various operations control and stages involved in a system with a help of graphic symbol. A flow chart thus, provides a concise and comprehensive view of what takes place in an organization, i.e. what documents are raised, how they are dealt with, what the flow of goods and cash is, what the various operations are, etc.

A flow chart enables one to understand even a complicated system easily. Lengthy narrative can often be confusing and unwieldy. A flow chart on the other hand, can depict the same situation in a simple and concise manner. Suppose a visitor to Delhi wishes to reach India Gate from the railway station. If the route is described to him by way of narratives, he may not be able to reach his destination on his own. This is because he will have to write down the names of a number of roads, places, and turnings. Also, he will have to comprehend the direction and connections of various roads and areas. Instead, a simple road map may be more helpful to him since he can follow exactly the directions indicated in the map. Similarly the utility of a flow chart lies in its capability of depicting not only the various phases of a system in a simple manner but also in showing their relationship and relative importance. A system which has various phases of varying importance with interconnection links can best be understood through flow chart.

An auditor requires certain specific symbols for all processes which have an effect on the internal control system. He may used are separate symbols for different types of operations such as signing or checking the totals, or comparison with basic document.

Preparing A Flow Chart – A Hypothetical Example

Suppose an auditor is preparing a flow chart regarding the purchases made by a manufacturing enterprise. Purchasing involves at least four different sections. i.e. stores, purchase department, goods receipts sections



and accounts. The basic stages are :-

1. Preparing requisition for requirement of materials.
2. Issue of orders.
3. Receipt of goods.
4. Payment to suppliers.

The depiction of all these four stages in one flow chart may result in the chart becoming too complicated and cumbersome. Hence the detailed procedure regarding payments to suppliers may be shown by a separate chart. The auditor will approach each person involved in the first three stages of the purchasing function and chart the procedure on the basis of information so obtained.

8.6 INTERNAL CONTROL – NATURE AND SCOPE

The system of internal control may be defined as “Plan of organization and all the methods and procedure adopted by the management of an entity to assist in achieving management’s objective of ensuring, as far as practicable, the orderly and efficient conduct of its business, including adherence to management policies, the safeguard of assets, prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information.” The system of internal control extends beyond those matters which relate directly to the functions of the accounting system.

In a financial audit, the auditor is concerned primarily with the accounting controls. In an operational audit, however, the auditor reviews all operational controls. From this point of view, internal controls can be classified into two broad categories : accounting controls and administrative controls.

Accounting Controls comprise primarily the plan of organization and procedures and records that are concerned with the safeguarding of assets, prevention and detection of fraud and error, accuracy and completeness of records, and timely preparation of reliable financial information. Administrative controls include all other managerial controls concerned with the decision-making process.

Significance and Objective of Control

For the administrative control and attainment of objectives of an organization, formulation of policies and procedures is a must. Such policies and procedures must be communicated to all levels so that accomplishment of objectives becomes a reality. To administer such a process of management, a business concept called “internal control” has been evolved. The importance and the manifold necessities of this term are as under :-

- (a) To control the operations particularly where the organizational structure has become complex and widespread.
- (b) To bring business functioning or activities within the broad formulated plans, policies, objectives and goals.
- (c) To bring to light any misuse or misappropriation of the company’s assets (whether of current or fixed nature) and to take corrective measures in safeguarding assets.
- (d) To take corrective measures whenever there are symptoms of weakness or flaws in the management of the business.
- (e) To ensure that operational controls are fully effective.
- (f) To assess the adequacy and accuracy of control measures.
- (g) To create appropriate climate for efficient organizational functioning.
- (h) To safeguard the interest of the organization as well as guarding against the dishonesty; temptations, apathy, lethargy and inefficiency of the “men at work” through proper effective control measures which will act as deterrents to the occurrence or happenings of unhealthy situations.
- (i) To prevent and detect frauds and errors.
- (j) To ensure adequacy and reliability of management information and control systems.
- (k) To ensure timely preparation and presentation of various reports for decision-making.
- (l) Efficient system of internal control saves the statutory auditor from an impracticable exhaustive audit.



- (m) Absence of or ineffective control will lead to chaos in the organizational working and will be damaging to the morale of the people working for the organization. This will in turn jeopardize the leadership in management.
- (n) Due to the growing complexity of running a business, management will have to depend on various reports, facts and figures for decision-making.

Internal Auditor and Internal Control

The internal auditor's objective is to evaluate the performance, methods and systems of working on a continuous basis. In order to help management as to the effectiveness of controls, the auditor is to report :

- (a) Whether there are signs or symptoms of breakdown of the control systems.
- (b) Whether necessary changes are warranted.
- (c) To make management control system more effective so as to ensure that results are obtained for which the controls are established.

The internal auditor while making appraisal and review will have to examine the following aspects :

1. Documentation and work-flow
2. Objective analysis of the business situation
3. Organization structure and charts.
4. Systems of communication.
5. Performance assessment
6. Internal check system.

Through the process of evaluation and appraisal, the internal auditor will contribute towards effective control practices.

Internal control would cover both internal checks, internal audit and other forms of control, internal auditing is to a great extent an appraisal and review of internal control as discussed earlier. Internal control embraces or comprises the whole system and procedure of managerial control of any nature, be it financial, non-financial or accounting.

"Internal Auditing is an independent appraisal activity within an organization for the review of operations as a service to management. It is managerial control which functions by measuring and evaluation of the effectiveness of other controls".

This goes to show that the very nature of internal audit functioning and objectivity is the appraisal and review of control measures.

Now it follows that internal control includes internal check, internal audit, organization and methods (O & M) study and other operational controls. But internal audit is not a part of internal check nor part of any accounting or financial control system. Internal control is broader than internal check and the latter is an essential element of internal control. In internal auditing the appraisal, review and evaluation have been to begin with the study of control because it is essential that there must be a complete knowledge of the management control system.

In an organization, it is a fact that such a situation seldom exists. Management usually look for someone who can assure them that control systems are being followed and tested regularly for their suitability so that management can act confidently in managing the business. This is so far the management side of the picture. Then the question arises as to the scope of appraisal by the internal auditor to aid management in keeping up confidence in running a business and in achieving organisational objectives, The internal auditor's function is to an extent the determination of effective control measures – he is to appraise and assess the extent of implementation of the management control system. He is to ensure as well as to assure management that control system are as effective as these are expected to be and thereby changing hopes and aspirations of the organization into accomplishments. The internal auditor in order to succeed in his objectives should also have the cooperation of others in the organization since it is on them that the efficiency of control measures depends to a large extent. So it naturally follows that the appraisal of performance of personnel is to be done alongside the appraisal of the control measures itself.

The pattern and degree of control may vary between organization to organization due to certain variable factors. These factors are again listed here for convenience :



- (a) Magnitude of Organisation
- (b) Facilities available
- (c) Nature of business operations
- (d) Type of business
- (e) Nature of organizational structure
- (f) Capabilities and future potentialities of personnel

Due to such variables, the formulation and effectiveness of control measures will not be the same in all the organizations. Because of this, the pattern of appraisal and recommendation by the internal auditor will also vary. Each situation, under which control measures are formulated, adopted and developed, must form part of the subject for separate study.

Internal Check and Internal Control

Internal check system is organized to achieve the following objects :-

1. To prevent the commission of any errors or fraud.
2. To prevent the misappropriation of cash or goods by keeping a check on the receipts and payments of cash and receipts and delivery of the goods.
3. To throw responsibility when the fraud or mistake is detected.
4. To detect a fraud or an error quickly and easily
5. To have an accurate record of all business transactions.

Auditor's Duty In Regard to Internal Check System

In the case of a big concern where there is a good internal check system the auditor may, to a great extent, presume the accuracy of the accounting. But he must not be negligent. He should apply a few test checks, i.e. he should check a few transactions here and there at random or check fully the accounts for a few months, and carry out a thorough check of the whole of a certain class of transactions taking place during that particular period, e.g. cash sales, or cash received or credit purchases during that period. In selecting certain transactions are representative and true specimens the auditor should see that such sample transactions are representative and true specimens of such entries throughout the year.

If he finds that there is no mistake and there is nothing to arouse his suspicion, he may presume that the accounts are correct. It must be remembered that in such a case, the auditor is not relieved of his responsibility. Therefore, it would be better for him to probe the matter thoroughly if there is the slightest suspicion. If later on, it is found that a fraud had been committed which the auditor failed to detect as he had not checked all the transactions, he would be held liable. The existence of a good internal check system reduces to a great extent the work of the auditor but does not reduce his liability. To what extent an auditor should depend upon the internal check system will depend upon his tact, skill, experience and judgement.

The internal check is said to have the following fundamental aims :

- (1) To pin down to definite persons responsibility for particular acts, default or omission, by the segregation of tasks.
- (2) To obtain confirmation of facts and entries, physical and financial, by the creation and preservation of necessary records.
- (3) To facilitate the "breakdown" of routine procedures so as to avoid bottlenecks and to establish an even flow of work.
- (4) To reduce to a minimum the possibility of fraud and error.

Check list is usually a questionnaire set, designed to draw attention to important aspects of the system of internal check. The question should be phrased in such a way that an affirmative answer would normally reveal a satisfactory position. If the answer is negative, enquiry should be made to see if there is a satisfactory substitute for the procedure referred to in the questionnaire. A negative answer always merits further examination. All the items on the questionnaire cannot be of the same importance and an unhealthy position might be revealed either by a single negative answer or by a number of such answers.



No questionnaire for the appraisal of a system of internal check can ever be considered to be complete. Although every effort should be made to make such a questionnaire as comprehensive as possible, it is primarily a stimulation to thinking along recognized channels.

Internal Control Questionnaires

The evaluation of internal check system in an organization is of great concern both to the statutory auditor as well as to the internal auditor. The guiding factor for audit operation by the statutory auditor depends to a great extent on the soundness or otherwise of the internal controls in business. Due to the limitation of time a statutory auditor can spend on a company's audit, he has to decide the extent of in-depth audit of many areas, particularly the checking and verification of routine aspects of financial transactions.

The evaluation of the internal check system including internal accounting control gives an opportunity to the statutory auditor to have a clearer insight into the operational systems and an overall view of the organizational workings to spot weakness in the systems and procedure both in respect of financial and operational areas of the business. The internal check system questionnaire is a list of systematically and logically prepared questions designed to find out and evaluate the effectiveness of the internal check system regarding various aspects and accounting transactions of an organization. The questionnaire are to be as comprehensive as possible in nature to make sure that all aspects and accounting transactions are covered which are to be replied by the official of the department or division concerned.

During the course of the audit statutory auditor will submit to the organization a complete questionnaire for reply by concerned official which will help the former to form an opinion as to the adequacy and reasonableness of the internal check system.

The statutory auditor during the course of his audit may make test checks or in-depth checking depending on the circumstances to make sure that the replies to the questionnaire are accurate and complete. In respect of many of the replies, the statutory auditor may have to make sure that the internal check system are really in operation through proper verification. In respect of negative replies, he may have to qualify his audit report depending on the seriousness of the situation.

The internal auditor in their pre-audit i.e. before taking up real internal audit operations may require the officials concerned to reply to the questionnaire. This will help the internal auditor in shaping his programming.

The department or divisional heads should also make use of such questionnaire, solely on their own initiative, by directing the personnel to prepare replies to such a questionnaire for the benefit of the department itself. This procedure will enable the department head to evaluate the existing internal control system and thereby to suggest management to review the said systems to further strengthen the organizational controls.

Internal Control Questionnaire For Cash And Bank Receipts

1. Is inward mail opened by persons not connected with handling cash or the Accounts Department ?
2. Is the inward mail date stamped ?
3. Is there a detailed record of receipts prepared ?
4. Are all cheques specially crossed by employees opening mail ?
5. Are bank deposits prepared and made by some one other than those responsible for cash receipts and/or personal ledger. Are duplicate (or counterfoils of) receipted deposit slips received from the bank ?
6. Is there any comparison of items listed on the duplicate (or counterfoils of) deposit slips with the amounts of cheques recorded in the cash receipts records ?
7. Are receipts given for over-the counter collections ?
8. Is there reconciliation of such proofs of collection with amounts banked?
9. Are collections of branch offices and sales offices deposited in special bank accounts subject to withdrawal only by the head office ?
10. If collections are made by representatives of the company in cash, have serially numbered been issued to them ?
11. Is there a system of issuing permanent receipts in lieu of the temporary/provisional receipts issued by bill collections etc.



12. Are such collections promptly received and banked? Are the receipts forms :
 - (a) Serially numbered ?
 - (b) Kept in safe custody ?
 - (c) Controlled by register ?
 - (d) Unused stocks checked regularly ?
 - (e) Made out by one employee and dispatched by another ?
 - (f) Accounted for, including those cancelled in respect of partially used receipts, books not intended to be used, cancelled. Are cancelled receipts preserved ?
13. Is the opening of bank accounts authorized by the Board of Directors ?
14. Are sundry items, such as, dividends, interest, rent, commissions etc. regularly checked by responsible official to satisfy that correct amount are received ?
15. Is there a procedure to ensure that Hundi borrowing as only by cheques crossed "Account Payee"?
16. Is the cash balance verified frequently (incoming money orders. VPP receipts etc.)
17. Are they listed immediately ?
18. Are such lists compared with the Cash Book regularly ?
19. Is there an arrangement with the postal authorities to receive cheques instead of cash ?
20. Are the cashier's duties taken over for a few days, by some one else, occasionally ?
21. If rough cash book is maintained :
 - (a) Is a fair cash book written up promptly ?
 - (b) Is the fair cash book checked with the rough cash book, by a person other than the cashier ?

Internal Control Questionnaire for Purchase And Creditors

1. Is purchasing centralized in the Purchase Department ?
2. Are purchases made only from approved supplier ?
3. Is a list of approved suppliers maintained for this purpose ?
4. Does the master list contain more than one source of supply for all important materials ?
5. Are the purchase orders based on valid purchase requisitions duly signed by persons authorized in this behalf ?
6. Are purchases made on behalf of employees ?
7. If so, is the same procedure followed as for other purchases ?
8. If special approval required for purchases from employees, Directors and Companies in which Directors are interested ?
9. Purchase of capital goods ?
10. Are purchases based on competitive quotations from two or more suppliers ?
11. Is comparative quotation analysis sheet is drawn before purchases are authorized ?
12. If the lowest quotation is not accepted, is the purchase approved by a senior official ?
13. If the price variation clause is included, is it approved by a Senior official?
14. Are purchase orders pre-numbered and strict control exercised over unused forms ?
15. Are purchase orders signed only by employees authorized in this behalf ?
16. Do purchase orders contain the following minimum information :
 - (a) Name of the supplier ?
 - (b) Delivery terms ?
 - (c) Quantity ?
 - (d) Price ?



- (e) Freight terms ?
 - (f) Payment terms ?
 - (g) Any extra applicable ?
17. Is revision of terms of purchase orders duly authorized ?
 18. Are copies of purchases orders and revisions forwarded to Accounts and Receiving Department ?
 19. If “yes” do the copies show the quantities ordered ?
 20. If “no”, is there an adequate procedure orders complied by Receiving Department to be notified to accept deliveries ?
 21. Is a List of pending purchase orders complied by purchase department at least office every quarter ?
 22. Are all materials, supplies, etc. received only in the Receiving Department. ?
 23. If they are received directly by User Department/Processors/ Customers, is there a procedure of obtaining acknowledgements for quantity received and the conditions of the goods ?
 24. Are persons connected with receipt of materials and the keeping of receiving records denied authority, to issue purchase orders or to approve invoices.
 25. Are materials, supplies etc. inspected and counted, weighted or measured in the Receiving Department ?
 26. Are quantities and description checked against purchase order (or other form of notification) and goods inspected for condition ?
 27. Does the Receiving Department deliver or supervise the delivery of each item received to the proper Stores or Department location.
 28. Are acknowledgements obtained from suppliers for goods/containers returned to them ?
 29. Are all receipts of materials evidenced by pre-numbered Goods Received Notes ?
 30. Are copies of Goods Received Notes forwarded to Accounts Department and a list of goods received to Purchase Department?
 31. Are all cases of materials returned, shortages and rejections advised to the Accounts Department, for raising Debit Memos on suppliers or claim bill on carriers/insurance companies as the case may be ?
 32. Are all debit notes :-
 - (a) Pre numbered ?
 - (b) Numerically controlled ?
 - (c) Properly recorded in the financial accounting or in memorandum registers ?
 33. Are all suppliers invoices routed direct to the Accounts Department ?
 34. Are they entered in a Bill Register before submitting them to other department for check and/or approval?
 35. Are advance and partial payments entered on the invoices before they are submitted to other departments?
 36. Does the system ensure that all invoices and credit notes received are duly processed ?
 37. In respect of raw materials and suppliers, are reconciliation made of quantities and or values received, as shown by purchase invoices, with receipts into stock records ?
 38. Are duplicate invoices marked immediately on receipts to avoid payment against them ?
 39. If payments are made against duplicate invoices even occasionally are adequate precautions take to avoid duplicate payments ?
 40. Does the Accounts Department match the invoices of suppliers with Goods Received Notes or acknowledgements received as per Q.17 and purchase orders ? Are Goods Received Notes and receiving records regularly reviewed for items for which no invoices have been received ?
 41. Are all such items, investigated and is provisions made for the liability in respect of such items ?
 42. Is such review/investigation done by a person independent of those responsible for the receipts and control of goods ?
 43. Do all invoices bear evidence of being checked for prices, freight terms extensions and additions ?



44. Is the relative purchase order attached to the invoice for payment ?
45. Where the client both buys from and sell to a person regularly, is a periodic review made of all amounts due from him to determine whether any set off is necessary ?
46. Is a special request used for making payments in advance or against documents through Bank ?
47. Thereafter, are the invoices processed in the normal course ?
48. Are all advance payments duly authorized by persons competent of authorize such payment ?
49. Is a list of pending advances made at least every quarter and is a proper follow up maintained ?
50. Are all adjustments to creditor's accounts duly approved by those authorized in this behalf ?
51. Is a list of employees by designation with limits of authority in respect of several matters referred to in this section maintained.
52. Are all suppliers statements compared with ledger accounts ?
53. Is there any follow up action to investigate differences, if any between the supplier's statements and the ledger accounts ?
54. Is a list of unpaid creditors prepared and reconciled periodically with the General Ledger Control accounts?
55. Is there a system of ensuring that cash discounts are availed of, whenever offered ?

Internal Control Questionnaire for Sales And Debtors Section

1. Are standard price lists maintained ?
2. Are prices which are not based on standard price lists, required to be approved by senior executive outside the Sales Department ?
3. Are written orders from customers received in all cases ?
4. If oral/telephonic orders are received, are they recorded immediately in the client's standard forms ?
5. Is there a numerical control of all customers' orders ?
6. Are credit limits fixed in respect of individual customers ?
7. Are credit limits approved by an official independent of the Sales Department ?
8. Are credit limits reviewed periodically ? Are customers' credit limits checked before orders accepted ?
9. Is this done by a person independent of Sales Department ?
10. If sales to employees are made at concessional prices ?
11. Is there a limit to the value of such sales ?
12. Is there an adequate procedure to see that these limits are not exceeded?
13. Are the amounts recovered in accordance with the term of sales ?
14. Are dispatches of good authorized only by Despatch Notes/Gate passes or similar documents ?
15. Do such Despatch Notes/Gate passes or similar documents bear preprinted numbers ?
16. Are they under numerical control ?
17. Are they prepared by a person independent of : the Sales Department ?
18. The processing of invoices ?
19. Except when all documents are prepared in one operation, are the Despatch Notes/Gate passes matches with:
 - (a) Excise Duty Records?
 - (b) Sales invoices (applicable)?
20. Are the goods actual dispatched checked independently with the Despatch Notes/Gate passes and Customer's Orders?
21. Are acknowledgements obtained from customer for the goods delivered ?
22. Are the Customer's orders marked for goods delivered ?
23. Are shortages in goods delivered to the customer investigated ?



24. Are credits to customers for shortage, breakages and losses in transit matched with claims lodged against carriers/insurers ?
25. Are all invoices pre-numbered ?
26. Are sales invoice numbers accounted for ?
27. Are invoices checked for price ?
28. Calculations including
 - (a) Excise Duty and sales tax ?
 - (b) Terms of payment ?
29. Are “no charge” invoices authorized by a person independent of the custody of goods or cash ?
30. Are invoices mailed direct to the customer promptly ?
31. Are credits to customer for remittances posted only from the entries in the cash book (or equivalent record)?
32. Does cashier notify immediately –
 - (a) Sales Department
 - (b) Debtors’ Ledger Section and
 - (c) Credit Controller –
 - (i) Of all dishonoured cheques or
 - (ii) Other negotiable instruments of all documents sent through bank but not retired by the customers?
33. Is immediate follow up action taken on such notification ?
34. Are bills of exchange etc. as per such record periodically verified with the bills on hand ?
35. Is record of customers’ claims maintained ?
36. Are such claims properly dealt with in the accounts ?
37. Does the Receiving Department count, weigh or measure the goods returned by customers ?
38. Does the Receiving Department record them on a Sales Returns Note ?
39. Are copies of Sales Returns Notes sent to
 - (a) Customer ?
 - (b) Sales Department ?
 - (c) Debtors Ledger Section ?
40. Are the returned goods taken into stock immediately ?
41. Is a Credit Notes issued to the customer for the goods returned ?
42. Are all Credit Notes pre-numbered ?
43. Are Credit Notes numerically controlled ?
44. Are Credit Notes authorized by a person independent of :
 - (a) Custody of goods ?
 - (b) Cash receipts ?
 - (c) Debtors’ Ledger ?
 - (d) Are Credit Notes –
 - (i) Compared with Sales Returned Notes or other substantiating evidence ?
 - (ii) Checked for price ?
 - (iii) Checked for calculations ?

Are corresponding recoveries of sales commissions made, when Credit Notes are issued to customers ?
45. Are units of sales (as per sales invoices)s correlated and reconciled with the purchases (or production) and stocks on hand ?
46. Is the Sales Ledger balanced periodically and tallied with the General Ledger control account?



47. Are ageing schedules prepared periodically ?
48. Are they reviewed by a responsible person ?
49. Are statements of accounts regularly sent to all customers ?
50. Are the statements checked with the Debtors' Ledger before they are issued ?
51. Are the statements mailed by a person independent of the ledger keeper?
52. Are confirmation of balances obtained periodically ?
53. Are the confirmation verified by a person independent of the ledger keeper and the persons preparing the statement ?
54. Is special approval required for payment of customers ?
55. Writing off Bad Debts ?
56. Is any accounting control kept for bad debts written off ?
57. Is any follow up action taken for recovering amounts written off ?
58. In the case of export sales, is a record maintained of import entitlements due ?
59. Does the record cover the utilization/disposal of such entitlement ?
60. Are sales of scrap and wastage subject to the same procedures and controls as sales of finished goods ?

8.7 FIELD WORK – COLLECTING EVIDENCE ETC

The internal auditors' duty is to collect, classify and appraise information so that he is able to form an opinion and to make necessary recommendations for effective improvement in operation of the business. This job would consume a larger part of the auditor's time.

Two factors are mainly involved in this work :-

- (a) Measurement
- (b) Evaluation

The Institute of Internal Auditors defines this field work as, "It is a managerial control which functions by measuring and evaluating the effectiveness of other controls".

First we shall discuss the concept of measurement. The internal auditor would be able to examine any operation in the company if he is able to grasp this concept.

He must examine the operations in terms of units of measurement and standards applicable in such cases. The units of measures would be some discreet elements e.g. the rupees, days, degrees, documents, machines and some other quantifiable material. So the units of measurement would be such by which success or failure of the operation can be judged objectively. The standards on the other hand are those quantities of acceptability with which the measured things may be compared.

Hence each audit job would have to be approached with the idea that it can be dealt with by :-

- (a) Determining its size, extent or other quality in terms of some units of measurement.
- (b) Comparison of the results with acceptable standards. Then only the auditor would be able to carry out the audit objectively and intelligently. If however, the audit job is such that it can not be approached as above, it would not be possible for the auditor to make an objective observation. In such cases perhaps he would be able to produce only some subjective observations.

It should be remembered that measures is only one aspect of the field work. After making the measures the internal auditor would have to evaluate the results. The auditor would have to evaluate the data obtained through measurements to form his opinion and recommendations. Evaluation would mean arriving at correct judgment and to express such judgment in terms of what is known. In a few cases monetary worth of something may be determined.

Measurement Standard

The auditor must be able to evaluate the standard as they are applied in the field work. The auditor may need some modification in the light of future changes. Standards which are developed yesterday might not be



applicable today. There may be some changes in the statutes, procedures, contracts etc For these reasons the standards have to be changed. The adequacy of the standards must be assessed.

The measures of standards by the auditor should be done from the point of view of quality, cost and time schedule.

Interviews

The internal auditor has to send his report to the management on the assigned areas. The report to be meaningful, informative and effective, has to be definite in every observation it contains. To have definiteness and authentication, sometimes the internal auditor “interviews” the functional people in an honest endeavor to have elucidation in respect of facts collected by him or his representative during the course of audit. In his report, the internal auditor would point out the facts observed by him during audit and would also mention the facts revealed during the interview for explaining the real position to the management.

Internal Audit Report is precious informative reports to aid the management in deciding the right course of action. Memoranda are often found very useful in passing some additional information to the internal auditor, in making his reports more informative and purposeful.

8.8 AUDIT NOTES AND WORKING PAPERS

Audit Note Book is a book, which is maintained by the audit clerk. During the course of audit, the clerk comes across several difficulties or new points, which he has to discuss with his seniors or auditor. He makes several enquiries which he thinks, have not been satisfactorily answered. Least he might forget, he notes down these points in a book which is called by different names such as Audit Note Book or Audit Memoranda. Such a book is written record of queries made, replies received thereto, correspondence entered into it. This book may be of great help to the auditor preparing his Audit Report from such a record. A separate Audit Note Book is maintained for each concern.

Some of the points which are noted down in an Audit Note Book are given below :-

1. A list of books of account maintained by the client;
2. The names of the principal officers, their powers, duties and responsibilities.
3. The technical terms used in the business;
4. The points which require further explanation and clarification;
5. The particulars of the missing vouchers, the duplicates of which have to be obtained;
6. The mistakes and errors discovered;
7. Totals or balances of certain books of account, Bank Reconciliation Statement;
8. Notes and queries which might be required at a subsequent audit;
9. The points which have to be incorporated in Audit Report;
10. Any matter which requires discussion with the senior or with the auditor;
11. Accounting method followed in the business;
12. Dates of commencement and completion of the audit;
13. Provisions in the Articles and Memorandum of Association affecting the accounts and audit.

If notes have been properly made in the Audit Note Book, it might prove to be of great value to the auditor later on, in case a suit is filed against him for negligence or misfeasance. Such a book will be a documentary evidence in favour of the auditor even after several years by which time the auditor might have forgotten everything about that particular audit. The importance of such Note Book was emphasized by Lord (then Mr.) Justice Vaughan Williams in the London and General Bank case. Similarly the Audit Note Book which contained detailed information was of great assistance to the auditor in the case of the City Equitable Fire Insurance Company.

Such a book should be clear, concise and complete so that it may be quite intelligible to the clerk who audit the accounts of the same concern next year. In fact it would be a guide to such a clerk.

**Audit Working Papers**

Working Papers are those papers which contain essential facts about accounts so that the auditor may not have again to go over the accounts of his client in case he wants to refer to them later on during the course of his audit e.g.,

1. Audit programme duly completed, showing the nature of work, the extent of checking and the initials of the persons who have done that work.
2. Working Trial Balance
3. The schedules of the debtors and creditors, fixed assets, investments etc.
4. Correspondence between the auditor and the debtors, creditors, bank etc.,
5. Certificate regarding Cash in hand and at Banks.
6. Certificate regarding the stock-in-trade, and its valuation;
7. Adjusting journal entries;
8. Abstracts from minute books;
9. Particulars of investments;
10. Particulars of depreciation;

OBJECTS OR AIM OF WORKING PAPERS

1. In order to support the auditor's report these papers show in detail the work performed by the audit clerks
2. The auditor can form an opinion about the efficiency or otherwise of the audit clerks.
3. As the working papers remain with the auditor, as we shall see later on, they are the permanent record and, therefore, in case of any suit against him for negligence, he can defend himself on the basis of these working papers.
4. The preparation of the working papers is a means to give training to audit clerks as to how to summarise the work done by them.
5. The working papers enable the auditor to point out to the client the weaknesses of the internal control system in operation, and deficiency of the accountancy system. He may therefore, be in a position to advice his client as to how to avoid such pitfalls.
6. The working papers help the auditor to plan for the succeeding year.
7. The working papers enable the auditor to prepare the report to be issued without much waste of time.
8. He can know that his assistants had followed his instructions.
9. If changes and transfer of staff are very frequent and in case such working papers exist the audit work can be assigned to others with minimum of dislocation with least possibility of duplication and omission of any work.
10. Future audit work can be carried on in the same sequence on the basis of the previous working papers.
11. Items left outstanding during the previous year, e.g. any document not produced, may be paid particular attention in the future.

Essentials of Good Working Papers

1. Completeness i.e. they should contain all the essential information so that they may be of maximum utility. Facts which are not important should be omitted.
2. Organisation and Agreements. The working paper should be so arranged that one may not find any difficulty in locating a particular matter. If they are not properly arranged it will entail loss of time in finding a particular fact while preparing the Report.
3. Clearness. The facts in the working papers should be set out clearly.
4. The facts stated should be readily apparent to the reader later on, e.g. schedules, where necessary, should be fully explanatory so that it will not be necessary to puzzle over the various sections.
5. Papers should be clearly fastened together, arranged in a logical order, properly and adequately referenced and the subject matter clearly marked on the top.



6. Sufficient space should be left after each note so that any decision taken by the auditor may be taken down in that space.
7. It is therefore felt that if audit working papers are handed over to the clients, an auditor may not be able to defend himself, if any dispute arises in future.

8.9 AUDIT REPORT

Audit report will be an indicator of the usefulness of the internal audit functioning in the organization.

TECHNIQUES OF EFFECTIVE REPORTING

Before setting out the report writing as well as in the process of report writing the following should be the guidelines :

- Clear thinking
- To whom the report is directed
- Purpose and aim of reporting
- At what stage the report writing to start
- Pattern of presentation
- Keep the reader uppermost in mind
- Translate technical matters to layman's language
- To visualize the reader's viewpoint
- Unbiased approach
- To mention the view point of the auditee
- Impact of the report or, in other words, what be the probable reaction to reporting whether action or decision will follow in quickest possible time or to be treated as of academic interest only.
- To remember the universal saying – “don't jump to conclusions”
- Facts and figures to be in proper sequences
- Cool and calm thinking to have logical and coherent presentation

Proper setting out of internal audit report can be significant if it contains complete and logically developed appraisal with ample background facts and figures. It will be heartening to note if the top management accepted the significance and importance of the internal audit report as a useful tool for future improvements.

The main factors to go into the consideration for the various ways of presentations of written reports are :-

- Nature of business of the organisation.
- Nature of subject or aspect appraised.
- For whom the report is intended.
- Purpose for which the report is prepared.
- Management attitude, directives and needs.
- Internal auditor's approach and caliber.
- Extent of emphasis on audit findings and recommendations.
- Extent of details required by auditee and management.

The usual modern trend in presentation of internal audit report is as follows :-

- Detailed report about the findings, observations and recommendation is submitted to the auditee.
- Aspects which are of minor importance do not appear in the “detailed report” but discussed with all concerned and action taken by the auditee for implementation. These aspects can take the shape of a letter form of report to record the recommendations and the implementation thereof.
- Matters of major importance and on which top management has to take action for implementation of the recommendations are reported as “highlights of the report’ to top management.”



REVIEW AND AUDIT OF INTERNAL CONTROL SYSTEM

Internal auditor convey his thought and action through discussion and reporting; internal audit reports to be effective, must comply with such fundamentals as : objectives, correctness, conciseness, clarity, courtesy, character (auditor must stand for what he believes), tact and timeliness.

An audit report should contain deficiencies, irregularities and scope for improvement as well as aspects which are efficient and effective.

One view is that the Internal audit reporting should follow the “principle of exception” i.e. the report should deal with only such aspects which are deficient and need improvements. Management cannot afford to spend time on matters which are in order.

Another view is that only reporting the deficiencies or irregularities without giving credit for aspects which are in order may damage the “selling the idea” approach or “advisory role” of the Internal auditor. This sort of reporting may even endanger the Internal audit objectives. In other words, both bad and good need to be reported otherwise the implementations of the recommendations may be adversely affected or delayed. In such a situation, it will be prudent that top management, operating management and the internal auditor must sit in a meeting to decide the pattern of Internal audit reporting. In significant reporting or the highlights of the reporting should be summarized briefly at the beginning of the report separately. By explaining findings in non technical language, the Internal auditor gets better results. Many executives have developed the habit of looking for summaries of report, conclusion and recommendations in summary form which will act as a snapshot of the entire findings of the report. The report should never give an impression of uninteresting, lengthy details of tediousness. The auditor should not get too engrossed in detail. Every effort is to be made to give a concise and to-the-point appearance to the report. Audit report should stimulate thought and action on the part of management and the operating personnel i.e. report is to infuse ideas to pave the road to solution of problems or inefficiencies.

Follow-up of Audit Report

Following are the aspects to be taken into account with regard to the follow-up of the Audit Report :-

- (a) Action taken on report-implementation of recommendations ;
- (b) Difficulties faced by auditee in implementing audit recommendations ;
- (c) Importance of follow-up.

The importance and necessity of follow-up arises due to the fact that human tendencies is “resistance to change” and to delay the adoption of audit recommendations. That is why, to reap the full benefits of audit, recommendations are to be implemented without any loss of time. The sooner the recommendations are put to action the better for all in the organization. Unless the observations and recommendations are considered, the objective of appraisal is dissipated. To avoid such unhealthy tendencies, the auditor will have to close and constant follow-up so that :

1. Challenging the validity of recommendations may receive due and timely attention by the auditor.
2. If the auditee finds practical difficulties in implementing audit suggestions may come out with his facts and figures for discussion with his superiors and the internal auditor.
3. Deficiencies and lack of control measures may be rectified without putting the organization into loss monetarily or otherwise.

To ensure that the recommendations being actually put into action, the internal auditor may have to pay a visit to the department/location, which is known as “follow-up visit” if the circumstances warrant.

It must be remembered, in this connection, that the auditor does not have line authority to enforce the recommendations. Hence, the auditor in the case of follow up has to act in an advisory capacity, i.e. auditor is to pursue that the recommendations are adhered to if the management so desired.

8.10 SUMMARY REPORT TO TOP MANAGEMENT

It may be the policy of the management to have copies of the Internal Audit Report in which there might be important findings. In such cases, the copy that might be endorsed to the top management should contain a



summary sheet giving gist of the audit report. It should be appreciated that top people are busy and have not much time to spare to go through the detailed report. The list should highlight the conclusion and the remedial suggestions to correct the deficient conditions.

The management would then be able to get an idea of the audit findings easily with minimum loss of time. The necessary details might also be referred to from the detailed report.

Summary reports to management usually would have two distinct functions –

- (i) They would tell what the internal audit department has accomplished when compared to what was planned.
- (ii) They would show conclusions of the auditors in a summarised form.

The significant ones may be advised to be corrected immediately, leaving the less important ones for taking action a bit later.

Such report should be under distinct subheads like the following :-

- (i) Major irregularities needing immediate attention.
- (ii) Routine irregularities of consequence.
- (iii) Case of supervisory lapses which may result in heavy loss etc.

In the first category irregularities like non-maintenance of stock account of receipt books, meeting departmental expenditure from cash collected in violation of the instructions in this regard may be included. In the second category may come non-posting of entries to make records like stock cards etc. up to date, non-reconciliation of control accounts with the subsidiary ledger etc.

In the third category may be included absence of supervisory check in the cash books, bill register, absence of supervisory percentage checking of the suppliers/contractors bill etc.

8.11 COMMUNICATION IN INTERNAL AUDITING

The Dictionary meaning of the word “Communication” is correspondence – a means of communicating – a connective passage or channel. The Internal Auditor remains engaged in auditing various functions and report on different segments of the business organization. His audit findings are reflected in the audit report which is submitted to the departmental heads as well as to the Chief Internal Auditor. These reports, therefore, serve as connecting channel between him and the authorities to whom such reports are submitted.

The Chief Internal Auditor and other auditors should, therefore, be well versed in the art of communication. Not only the auditors submit the report, they are also required sometimes explaining some matters included in the Audit Report – sometimes offering clarification to the recommendation made in the audit report etc.

Improving The Auditor-Auditee Relationship

It may be appreciated that for carrying out internal audit functions properly and efficiently, there should be a cordial relationship between the Auditor and the Auditee.

The maintenance of good relations between the two would, however, be like a two way traffic. The auditor must keep in mind that he is to sell a product viz the audit service and the customer i.e. the management must be ready to accept the product if it is of standard quality. If the management is really interested in improving the efficiency of the business operation by utilizing this important management tool “(Internal Audit)”, it must appreciate and take action on the Internal Audit Report and findings, if however, the products of audit are useful.

The Internal Auditor’s campaign must be aggressive and dynamic. Each audit performed in traditional financial area must be thorough and sound. Each audit report should show the imprint of professional quality both in terms of form and substance. Such audit report would be more useful to the management if the audit is carried out keeping in view the management’s view point. It may, therefore, be said that even in the traditional, financial accounting area there is scope for improvement of the audit products.

If the Internal Audit Department can continue its effort in making the audit report more attractive, by carrying out audit keeping in view the management’s requirements, the cordial relationship between the two, that has once grown would continue providing newer scope to the Internal Audit Department for offering better service to the management.



8.12 SCOPE OF AUDIT COMMITTEE

An Audit Committee consists of three to five members formed to serve as communication link among various departments. Audit Committee has a four fold relationship and therefore has to interact with management, internal auditor, statutory auditor and the public.

The Scope of Audit Committee can be discussed as follows :-

- (i) Review of annual financial statements before submission to the Board of Directors.
- (ii) Selection of the Statutory Auditor
- (iii) Act as lies on between the Statutory Auditor and Board of Directors
- (iv) Administrative control of the internal control functions through the feedback between the Internal Auditor and the Audit Committee.
- (v) Over seeing internal central operation.
- (vi) Over seeing internal audit operations and feedback between internal audit committee and developing the internal auditing authority through broad based internal audit programming.
- (vii) Review and approval of financial information for publication
- (viii) Review proposed changes in accounting system and procedures.
- (ix) Help resolve differences between management, internal and statutory auditor.
- (x) Report on the audit committee acting in the Annual Reports of Board of Directors.
- (xi) Ensure reliability of organisation's financial statements and operational activities.

To be effective and purposeful, the audit committee should maintain the following :-

- (a) Audit Committee should have the independence of management, Statutory Auditor and Internal Auditor. The Board of Directors allow full freedom to the audit committee to investigate into any areas of operation.
- (b) The relation between the audit committee and management should be cordial and congenial towards optimum efficiency and healthy growth of the organization.
- (c) There should be a regular line of communication through occasional meetings with the management.
- (d) There should be good communication relationship interwoven among management, internal auditor and Statutory auditor.

8.12 INTERNAL AUDIT AND THE INVESTIGATION OF FRAUDS

In the minds of the public at large and of many clients, the discovery of frauds is the principal function of the auditor, overshadowing his other duties entirely, and although this is far from correct, there can be no question that it is of great importance.

Fraud may be divided broadly into two classes -

- 1. Defalcation, involving either misappropriation of money or goods.
- 2. The fraudulent manipulation of accounts not involving defalcation.

As regards the first, where accounting staff are not subjected to any form of check, the opportunities of committing fraud are so frequent, and the methods necessary to conceal it so comparatively simple, that it is safe to say that no business of any size could be carried on under such conditions for very long without the risk of fraud taking place. In small business where the individual proprietor is in touch with the whole of the detail, and is able to supervise it effectively, the possibilities of concealing fraud may be remote. As soon, however, as the business increases in size and the proprietor is no longer able to do this the a check is to be carried out by members of the staff themselves assisted by an independent auditor. Where the staff is sufficiently large to enable the whole of the work to be sub-divided, the auditor should examine carefully the system in force and ascertain it's deficiencies, if any.

The auditor, should pay particular attention to those classes of transactions which offer scope for fraud, the principal of which are cash transactions of one kind or another.



As general principles only are under consideration here, the actual way in which these transactions should be verified will be dealt with in due course but it may be noted that there are two methods by means of which the misappropriation of money may be concealed, the first is by the inclusion of fictitious payments, and the second by the omission of cash received, the latter class being much more difficult to detect.

The second class of fraud entailing the falsification of accounts without corresponding defalcations, is naturally considerable less frequent than the class of fraud above mentioned, but when it does occur it may involve very large amount. It may be done for the purpose of bolstering up a business which is in an insecure condition, in order to maintain the confidence of shareholders, creditors or the public; or it may be done by a manager for the purpose of increasing the apparent profit of the business, thus showing that he has been successful in his management, and possibly increasing the commission on results payable to him; or by directors for the purpose of enabling them to pay dividends which would otherwise not have been possible. Several notable cases of this sort of falsification have occurred. It need only be pointed out here that this form of fraud is often very ingeniously and skillfully concealed, and is in many cases carried out by persons holding positions of the highest trust, and having the entire confidence of directors and shareholders.

The Internal Audit Department has a big role to play in preventing fraud in different organizations, as a part of protective functions. Every big organization has an internal audit manual and such a manual usually outlines the internal audit function in detail vulnerable areas where loss through fraudulent means may arise frequently. Examples of vulnerable areas are stores receipt/consumption, Cash expenditure, sizeable receipts of cash, civil maintenance jobs etc. The internal audit manual prescribes in detail the manner and procedure as to how internal audit function would be carried out in these areas. The manual also directs the frequency of such audit. If internal audit of such areas is done accordingly, the possibility of occurrence of both visible and invisible frauds get eroded.

In discharging his functions in sensible areas as mentioned aforesaid, the auditor has to be extra intelligent and imaginative to enable him to think ahead of many others. However, it needs to be mentioned that the success of internal auditor in preventing fraud is also depending on the cooperation from other departments of the organization.



Study Note – 9

INFORMATION SYSTEM AUDIT AND MANAGEMENT AUDIT

This study note includes

- **Information System Audit**
 - Information System Audit
 - Computer Auditing
 - Computer Information System & Environment
 - Computer Information System and Internal Control
 - Audit Risks
 - Steps in an Audit
 - Computer Assisted Audit Techniques
 - Auditing in a Computerised Information System (CIS)
 - Audit in the case of EDI
 - Audit in case of E - Commerce Environment
 - Audit in Online system Environment
 - Audit in the case of Environment of personal computer
 - Audit in case of data processing.
- **Introduction To Management Audit**
 - Definition
 - Need
 - Scope
 - Management Audit Process
 - Advantages of Management Audit
 - Limitations of Management Audit

9.1 INFORMATION SYSTEM AUDIT

Formerly the information system audit was called as Electronic Data processing (EDP) audit. Information System Audit is also known as Informational Technology Audit.

The information technology audit was introduced in mid 1960 and has gone through numerous changes due to advance in technology and the incorporation of technology into business.

(A) Information System Audit

When it is an information technology audit the auditor is required to have a detailed knowledge of information system and alongwith a general understanding of accounting.

System

System means the instrumentality that combines interrelated interacting artifact designed to work as a coherent entity.

Information- It is a knowledge derived from study, experience or instruction in simple words. Information is message received and understood.



Information system or Information Technology Audit

It is an examination of the control within an information technology infrastructure. These receivers may be performed in conjunction with a financial statement audit, internal audit or other from of attestation engagement. This is a process of collecting and evaluating evidence of an organisations information systems practices and operations. The evaluation of obtained evidence determines if the information system are safeguarding assets, maintaining data integrity and operating effectively and efficiently to achieve the organisation's goals or objective. The information technology audit is also known as automated data processing (ADP) audit and computer audit.

Purpose

An I.T. audit is not entirely similar to that of a financial statement audit. An evaluation of internal control may or may not take place in an I.T. audit. Reliance on internal control is a unique characteristic of a financial audit. An evaluation of internal controls is necessary in a financial audit, to place reliance as on internal control and therefore substantially reduce the amount of testing necessary to form an opinion regarding financial statement of the company. An I.T. audit may take the form of a "Central control review" or an "Application control review". The review of different control measures by using different audit tools to examine system programming and data central procedure in order to determine the efficiency of computer operation, such as data base central, Encryption tools, fire wall tools, forensic tools, NEWS, NMAP, steganography tools, VOIP tools, War driving tools, WEP cracking tools, Wireless tools etc.

Regarding the protection of information assets, one purpose of I.T. audit is to review and evaluate an organisations information system availability, confidentiality and integrity by answering question like -

- (1) Will the organisations computer system be available for the business of all times when required (Availability)
- (2) Will the information in the system be disclosed only to authorised users (Confidentiality)

Approach

There are three systematic approaches to carry out an I.T. audit which are -

- (a) Technological Innovation Process Audit :

The aim of this approach is to construct a risk profile for existing and new project by asserting the length and depth of company experience in it.

- (b) Innovative Comparison Audit.
- (c) Technological Position Audit.

This review the technologies needed by the business and places them in one of the four categories of base, key, packing and emerging

Types of I.T. Audit

- (1) System and Application

An audit to verify that system and application are appropriate, efficient and adequately controlled ensure valid, reliable, timely and secure, input, processing and output at all levels of a system activity

- (2) Information Processing Facilities

An audit to verify that this processing facility is controlled to ensure timely, accurate and efficient processing of applications under normal and potentially disruptive conditions.

- (3) Systems Development

An audit to verify that the system under development meet the objectives of the organisation and to ensure that the systems are developed in accordance with generally accepted standards for system development.

- (4) Management of I.T. and Enterprise Architecture

An audit to verify that I.T. management has developed an organisational structure and procedures to ensure a controlled and efficient environment for information processing.

- (5) Client

Tele communicator, Internets, Extranets



An audit to verify that controls are in place on the client, server and on the network connecting the client and server.

As in case of other audits, the IT audit process too take the following basic steps -

- (1) Planning.
- (2) Studying and Evaluating control.
- (3) Testing of evaluating control.
- (4) Reports.
- (5) Follow up.

(B) Computer Auditing

In information processed on computers the one way of auditing is to get the printouts of all records, accounts and information and then check it as usual, but this is very time consuming and cannot evaluate the system of internal controls and certain errors found etc, remains undetected. The other more acceptable way is to evaluate the controls in the computer information system and then decide the nature of timing and extent of the substantive procedure to be followed and make use of computer in conducting compliance tests as well as substantive test, but and the auditor must have sufficient knowledge of computer system even in certain of cases specialised skills in operations of computer system.

(C) Computer Information System

The computer information system environments may be different in cases of different computer system used and there are certain common features of all computer information systems environment, like.

Organisation Structure :-The organisation structure includes knowledge, programme, data & different kinds of jobs at one place.

Nature of processing : Sometimes without having any document as a base, some particular transactions like interest directly credited to particular account by the system itself as per the programme instruction. Apparently in computerised accounting unlike manual accounting the transaction trials are not available but auditor can find it in machine readable form. Unless appropriate control are installed, there is a great possibility of unauthorised access to the computer system. Unless appropriate control are installed the data can be accessed and altered through terminals from remote locations.

Designs : The computer information system work more consistently because computer performs exactly according to its program. A program can incorporate automatic checks, which locate abnormal transactions and get included in a report to be reviewed by the concerned officer. Password techniques is used to avoid unauthorised access. A Single transaction entered in the system automatically makes entry in all related records. The program installed in the system, initiate particular transaction on its own. The program and data is stored on hard disc or any other portable media like CD, floppy etc. which can face intentional or accidental destruction.

(D) Computer Information System And Internal Controls

An auditor is concerned with the control from the point of view of authenticity, accuracy, completeness, assets safeguarding etc. Though the internal control in computer information system are based on the principles same as those followed in manual system which means the system of authorisation and allotment of duties etc. are determined on the same basis as in the manual system.

Some of these controls are as under -

- (1) **Password** - This control is used to identify the person before the computer information system starts processing the task. This control assures that the data fed into and the processing done by the computer information system are authorised.
- (2) **Edit Test** - Edit test, Financial control test etc. help in correct data entry and the accurate processing by the computer information system.
- (3) **Batch Cancellation Stamp** - This control keeps check on the processing of data only once and the repetition is avoided.



- (4) **Financial Control Total** - Along with edit test, this control helps in saving of the data and complete processing of the data.
- (5) **File Libraries** - File libraries, locks on computer installation etc. are used to safeguard the computer information system from destruction and corruption.
- (6) **Audit Trails** - Ensures that all those record and process are maintained within the system from which financial statement are derived.
- (7) **General Control** - These control establish overall control of the activities of computer information system. These controls include a) Organisational Control b) System & Documentation Control c) Access Control d) Hardware Control e) Procedural Control etc.
- (8) **Application Controls** - Over and above general control, control over the application of the computer information system is very important. These controls include a) Input control b) Processing control and c) Output control

The Auditor should evaluate the above control measures to ascertain the effects of them on the system. A clear audit trail assists the auditor to audit on it, allows the Auditor to trace the transaction from input to output data. The proper electronic trail helps in tracing the transaction properly.

(E) Audit Risks:

Information System Auditor is concerned with following objectives-

- (a) Asset Safeguarding
- (b) Data Integrity
- (c) System Effectiveness
- (d) System Efficiency

Auditor collects necessary evidences to assess whether the audit achieves the above objectives, but due to the nature of verification, auditor might fail to detect real material losses or errors. To reduce this risk, the appropriate audit approach is selected and is designed accordingly. The American Institute of Certified Public Accountants in 1988 determined the level of audit risk to be adopted by using the following 'Risk-Model'.

Desired audit risk - Internal risk X Control risk X Detection risk.

Internal risks represent the material loss or errors existing in some segment of the audit, before the reliability of internal controls is considered.

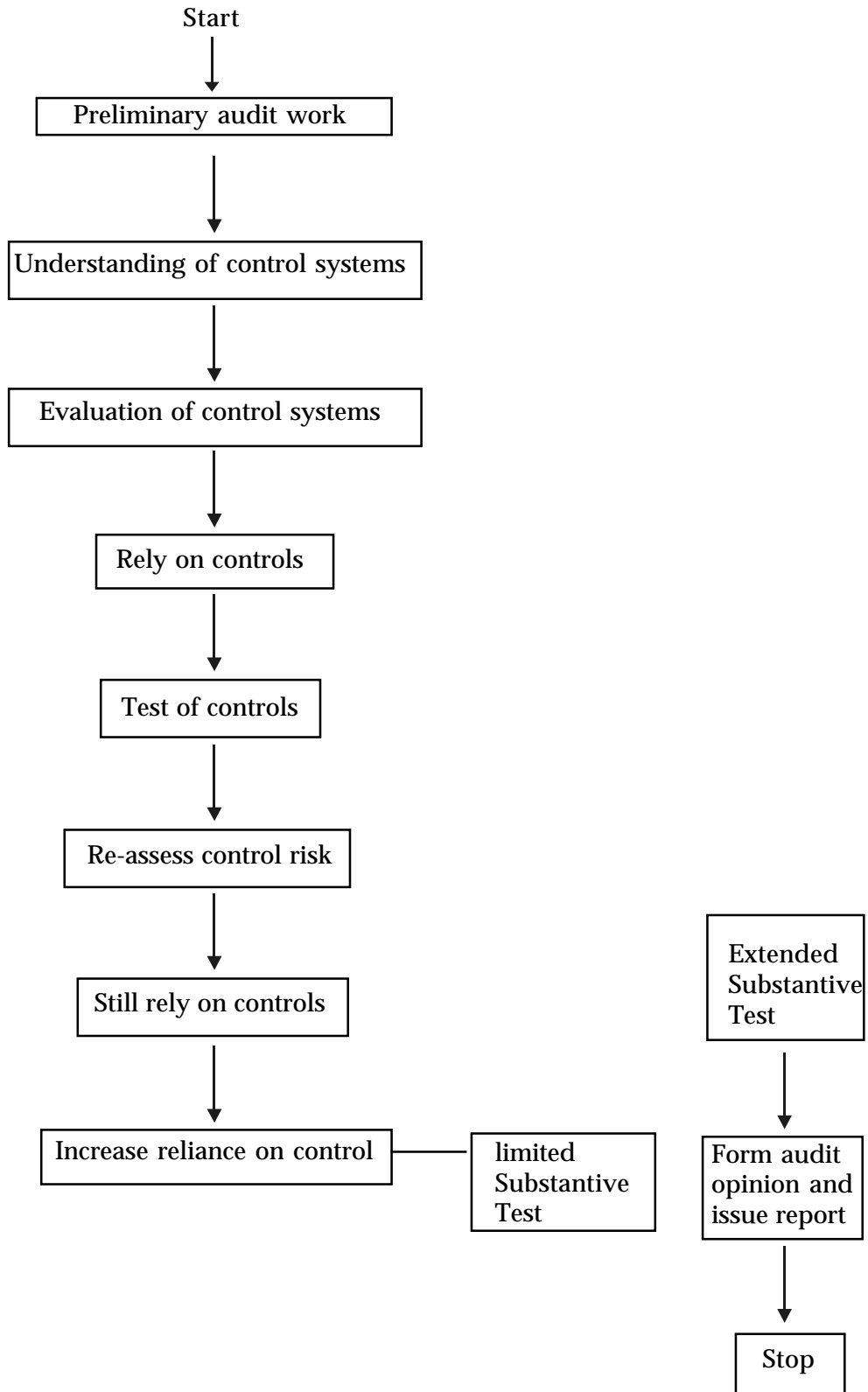
Control risk means the likelihood of internal controls in some part of audit can not present, detect or correct the material losses or errors.

Detection risk means the audit procedures used in some part of audit will fail to detect the material losses or errors.

While applying this model auditor select his level and desired audit risks, along with that he assures the short term and long term consequences upon the Auditor of the material losses and errors, he fails to detect. Afterwards, an auditor considers the internal risk in which he takes into consideration the nature of organization, the industry in which it operates the nature of management and accounting system and application systems. To evaluate the level of control risk, auditor considers the reliability of management and application controls, which include management controls which cover all the application systems and if it is absent it is a serious concern for the auditor. Lastly, auditor calculates the level of detection risk and for that he designs procedures for evidence collection on the basis of his understanding of how likely this procedure is to detect the existing material losses and errors and while designing the audit procedure he must ensure that it is properly executed. In short, the audit risk model is an effort focused on the areas where the auditor has the highest payoffs, in most cases he cannot collect sufficient evidence and hence he must be clear in mind in terms of where he applies this audit procedure and how he interprets the evidence. Auditor, throughout the audit, makes decisions on what to do next and his notions of materiality and audit risk guides him in making the decision.

(F) Steps in an Audit

After understanding the importance of system factoring to reduce complexity, the nature of audit risks and its consequences, the types of audit procedure, auditor can carry out actual audit as shown in the following flowchart as the approach advocated by the American Institute of Certified Public Accountants in 1990.





Both external and internal auditors will follow the above approach, the decisions they take at each step may vary because of having different rules like internal auditors may spend more time than the external auditors in testing controls as they are more concerned with the efficiency of the controls.

(G) Computer Assisted Audit Technique (CAAT)

Computer assisted audit technique uses computer to process the information, required for audit, stored in the auditee's information system. This technique is used for testing general controls and application controls and also for substantive procedures. This technique is also helpful in getting data from auditee's record as well as for analytical procedures.

The auditor must have expertise and experience in executing and using the results of the Computer Assisted Audit Technique. Before applying this technique auditor should get reasonable assurance of its integrity, reliability, usefulness and security through appropriate planning, designing, processing and review of documentation. He should see that this technique is properly controlled. Auditor should maintain sufficient documents describing the application of the technique and regarding planning, execution, inputs, processing, output, source code, technical information about the auditee's accounting system, audit evidence and suggestions, if any, for use of the technique in future etc. Auditor should make necessary arrangements for data files to minimize the effect on auditee's routine activities.

Different Computer Assisted Audit Techniques available are as under.

- (a) Test data
- (b) Integrated Test Facility
- (c) Audit Software
- (d) Audit Automation
- (e) Core Image Comparison
- (f) Data Base Analysis
- (g) Embedded Code
- (h) Log Analyzers
- (i) Mapping
- (j) Modeling
- (k) Online Testing
- (l) Program Code Analysis
- (m) Program Library Analyzers
- (n) Snapshots
- (o) Source Comparison
- (p) Tracing

(H) Auditing in Computer Information Systems

(Approach to Information Systems Audit)

The overall objective and scope of audit is not different in computer information system environment but the use of computer changes the processing, storage, retrieval and communication of financial information and also affects the accounting system as well as internal control system used by the auditee. The CIS environment may affect –

- a. The procedures followed by the auditor in obtaining a sufficient understanding of the accounting and internal control system.
- b. The auditor's evaluation of internal risk and control risk through which the auditor assesses the audit risk.
- c. The auditor's design and performance of tests of control and substantive procedures appropriate to meet the audit objective.

The auditor should consider the following to determine the effects of computer information system environment on the audit-



- a. The extent to which CIS environment is used to record, compile and analyze accounting information.
- b. The system of internal control in existence in the entity with regard to-
 1. Flow of authorized, correct and complete data to the processing centre.
 2. Processing, analyzing and reporting tasks undertaken in the installation.
- c. The impact of computer based accounting system on the audit trial that could otherwise be expected to exist in an entirely manual system.

The auditor should have sufficient knowledge of the computer information systems to plan, direct, supervise, control and review the work preformed. The sufficiency of knowledge would depend on the nature and extent of the CIS environment. The auditor should consider whether any specialized CIS skills are needed in the conduct of the audit. These specialized skills are needed to—

- a. Obtain sufficient understanding of the effects of the CIS environment on accounting and internal control systems.
- b. Determine the effect of the CIS environment on the assessment of overall audit risk and of risk at the account balance and class of transaction level.
- c. Design and perform appropriate tests of control and substantive procedures.

The inherent risks and control risks in a CIS environment may have both a pervasive effect and an account-specific effect on the likelihood of material misstatements, as follows:

- (a) The risks may result from deficiencies in pervasive CIS activities such as program development and maintenance, system software support, operations, physical CIS security, and control over access to special-privilege utility programs. These deficiencies would tend to have a pervasive impact on all application systems that are processed on the computer.
- (b) The risks may increase the potential for errors or fraudulent activities in specific applications, in specific databases or master files, or in specific processing activities. For example, errors are not uncommon in systems that perform complex logic or calculations, or that must deal with many different exception conditions. Systems that control cash disbursement or other liquid assets are susceptible to fraudulent actions by users or by CIS personnel.

As new CIS technologies emerge for data processing, they are frequently employed by clients to build increasingly complex computer systems that may include micro-to –mainframe links, distributed databases, end-user processing, and business management systems that feed information directly into accounting systems. Such systems increase the overall sophistication of computer information systems and the complexity of the specific applications that they affect. As a result, they may increase risk and require further consideration.

The Auditor should consider C.I.S environment while designing audit procedures to reduce audit to an acceptably low level. He should make enquiries and particularly satisfy himself whether :

- (a) Adequate procedures exist to ensure that the data transmitted is correct and complete.
- (b) Cross-verification of records, reconciliation statements and control systems between primary and subsidiary ledgers do exist and are operative and that accuracy of computer compiled records are not assumed.

The auditor's specific audit objectives do not change whether accounting data is processed manually or by computer. However, the methods of applying audit procedures to gather evidence may be influenced by the methods of computing process. The auditor can use manual audit procedures, or computer-assisted techniques, or a combination of both to obtain sufficient applications, it may be difficult or impossible for the auditor to obtain certain data for inspection, inquiry, or confirmation without computer assistance.

The auditor should document the audit plan, the nature, timing and extent of audit procedures performed and the conclusions drawn from the evidence obtained. In an audit in CIS environment, some of the audit evidence may be in electronic form. The auditor should satisfy himself that such evidence is adequately and safely stored and is retrievable in its entirety as and when required.

(I) Audit In The Case of Electronic Data Interchange (EDI)

EDI means transfer of structured data between organizations in electronics form. This is widely used in western countries and expected to grow in India too within a very short period. This transfer is done on the basis of



certain accepted standards having legal base, like EDI FACT standard. Audit in such situations really requires advanced knowledge of computers. To establish the authenticity of the data exchange and also of the parties exchanging data the digital signatures are used, in this case it is extremely difficult to forge digital signature. These signatures are created and verified by the computer programs. The Information Act, 2000 has laid down legal framework for digital signature and electronic records.

Auditor, with usual procedures, should give consideration to the following aspects while auditing in case of electronic data interchange environment :

- (a) There should be detailed and clear cut agreement for electronic data interchange, between the concerned parties. There should be clear provision for ordering, delivery, acceptance, rejection of interchange of electronic data. It is also clearly mentioned in the agreement that the supply of electronic data through this interchange system shall have the same effect on an ordinary supply made on the basis of a purchase order.
- (b) There should be full proof controls in the system to avoid modifications in the data by third party while the data interchanged is in transit and for encryption, i.e. mixing of data and making it unreadable to third party, is used and the receiver can decrypt the data for his use.
- (c) Due to the in built control in the EDI system the recipient acknowledges the receipt of the data and in his confirmation certain key information of original data is repeated.
- (d) The parties exchange the logs frequently and used for logging the receipted and sent data, this proves helpful and nobody can deny the receipt or transmission of data.
- (e) To avoid adverse effect on the business due to failure of hardware, proper controls for contingency planning are introduced in the EDI system.

(J) Audit in the Case of E-commerce Environment

E-Commerce denotes the buying and selling transactions through internet using computers. It may pose certain difficulties in accounting, revenue recognition etc. While accounting in such e-commerce environment, an auditor should consider the following guidelines contained in the International Auditing Practical Statement :

- (i) Evaluate the changes in the auditee's business environment as an effect of e-commerce.
- (ii) Examine the business risk affecting the Balance Sheet due to e-commerce transactions.
- (iii) The officers including chief information officer are enquired to get the real picture of e-commerce and its effect on the state of affairs of the auditee.
- (iv) Evaluate the extent of risk addressed by the auditor due to use of e-commerce.
- (v) In case the auditee is using services of an Internet Service Provider, certain records of such service providers relating to the auditee be asked for and verified.
- (vi) Measure the risk involved in e-commerce transactions in the case of use of public network.
- (vii) See whether appropriate accounting policy is adopted for recording development costs and revenue recognition.
- (viii) Verify the non compliances of taxation and legal matters in the case of international ecommerce.
- (ix) Verify the controls established to reduce the risk associated with e-commerce transactions.
- (x) Verify the efficiency of physical, logical and technical controls established for authorization, authenticity, confidentiality, security for information etc. e.g. passwords, firewalls, encryption etc.
- (xi) Evaluate the reliability of the system to check the completeness, accuracy, timeliness and authorization of information.
- (xii) See that adequate controls regarding validation of input, prevention of transactions to be omitted or duplicated, acceptance of terms of agreement before order processing, prevention of acceptance of order if all steps are not completed by the customer, ensuring proper distribution of transaction details across multiple systems in a network and ensuring the retention of backup and security of the related record.

(K) Audit in Online System Environment

In online computer system the data stored on a central computer can be used by number of persons through the number of terminals. In some organizations distribution system is used where in computers are distributed



throughout the network and data processed at various stages. In some online systems, computer files are updated to give immediate effect to the transactions entered through terminals; this is called as online real-time system. The controls used in such systems depend upon the specific hardware and software used.

The auditor, while auditing in such environment should consider the following points –

- (i) He should get acquainted with the computer network, entry points from other organizations and for collecting the network diagram.
- (ii) He should review the network control system.
- (iii) He should verify whether proper control measures are in use to avoid unauthorized transactions, unauthorized changing in the data or program.
- (iv) He should review the internal controls as source documents are not available for every transaction, processing results are not available in printed form, and the reports required by the auditor are many times not available in printed form.
- (v) He should see into the procedures to ensure proper authorization of data fed into the computer.
- (vi) He should insist upon the retaining of important links in audit trails.
- (vii) He should verify the effectiveness of separating the transactions accounting period wise to avoid confusion in the situation of overflow of online transactions.
- (viii) He should see that proper measures like establishment of appropriate controls to detect and correct line errors, cryptographic controls etc. are introduced in the system effectively to avoid the loss of data by accident or corruption.
- (ix) He should test the sample transaction derived at random from the addition of audit instructions to the programs used in data processing for continuous monitoring the system.

(L) Audit in the Case of Environment of Personal Computer

The environment where in personal computers are used is different from the environment where in large computers are in use and that is why auditor has to adopt different approach to audit in such environment. According to the guideline issued by International Federation of Accountants, the auditor has to consider following points while conducting audit in such environment of personal computers :

- (i) He should understand that P.C.s generally do not have controls as many as those in large computers, the program and data can be saved on portable media like C.D.s and also on hard disk. The storage media is prone to accident. Portable storage media are also subject to damage or theft or misplacement.
- (ii) He should know that inadequate control measures can create serious problems like theft or alteration of data due to unauthorized use of P.C.
- (iii) He should see whether proper controls are introduced to avoid unauthorized use of P.C.s, downloading data, improper documentation, improper use of storage capacity etc.
- (iv) He should ensure that software are not subject to manipulation.
- (v) He should examine the control procedure like cross checking the results, testing of application programs, documentation of processed data, and range test of data to strengthen the software and data integrity.
- (vi) He should verify whether proper arrangement is made for back up copies of all data and important programs.
- (vii) He should concentrate on substantive tests and not waste his time in detailed examining of the computer information system's controls effectiveness.
- (viii) He should use computer assisted audit techniques.
- (ix) He should examine larger samples of transactions.
- (x) He should verify the effectiveness of different control measures utilized and report about that.

(M) Audit in the Case of Data Processing through Computer Service Centers

Small organizations get their data processed through computer service centers due to their incapability of investing huge amount in establishing the computer systems. In this case the organization provides documents to service center, which processes it and hands over the final output documents.



In such circumstances auditor should :

- (i) Verify that the vendor is reliable and suitable having the skills, experience and reputation.
- (ii) Evaluate the suitability of the contracted terms with regard to fixed cost, variable cost, the scope & timing of audit activities, the service center's responsibility in terms of maintaining data integrity and providing suitable back up and recovery.
- (iii) Check the compliance with the terms of contract.
- (iv) Seek to ensure that his ability to collect and evaluate evidence in relation to the attainment of the objectives of outsourcing is not inhibited.

The Impact on auditing is as follows :

- (i) Wide spread end user computing could sometimes result in unintentional errors creeping into systems owing to inexperienced persons being involved. Also coordinated program modifications may not be possible.
- (ii) Improper use of decision support systems can have serious repercussions. Also their underlying assumptions must be clearly documented.
- (iii) Auditor's participation to a limited extent in systems development may become inevitable to ensure that adequate controls are built in.
- (iv) Usage of sophisticated audit software would become a necessity, since conventional methods of auditing would no longer be sufficient.
- (v) The move towards paperless electronic data interchange would eliminate much of the traditional audit trail, radically changing the nature of audit evidence.

The rapid advancements in information technology would no doubt have a dramatic impact - on auditing. Auditors must adapt themselves to the changing environment much and acquire necessary additional skills.

9.2 INTRODUCTION TO MANAGEMENT AUDIT

(A) Definition

Management audit is the audit to examine, review and appraise the different policies of the management on the basis of certain prescribed standards. It is not like a traditional audit but is a comprehensive and critical review of all aspects of management performance.

"The Management Audit may be more specifically defined as being an investigation of a business from the highest level downwards in order to ascertain whether sound management prevails throughout, thus facilitating the most effective relationship with the outside world and the most efficient organization and smooth running internally"- Taylor and Perry.

"The Management Audit is an informed and constructive analysis, evaluation and series of recommendations regarding the broad spectrum of plans, process people and problems of an economic entity"- Camp Field.

"The Management Audit may be defined as a comprehensive and constructive examination of an organization structure of a company, institution or branch of Government or any component thereof, such as a division, or department, and its plan and objectives, its means of operation and its use of human and physical facilities."- William P. Leenard.

In short the Management Audit is a forward looking audit. It emphasizes on problem identification rather than problem solving, it pinpoints the areas requiring attention of management, it evaluates the existence of well defined objectives and examines whether policies are consistent with objectives and understood properly at all functional levels, it goes far behind the areas of financial accounting and cost accounting, it seeks to review, appraise and evaluate the corporate plans and policies based on certain standards of objectivity. Though this type of audit is made mandatory in Sweden and USA, it is yet to take appropriate momentum in India.

(B) Need of Management Audit

The following are the circumstances wherein the management audit is useful-

- (i) To overcome the human limitations of Top Management.



- (ii) To improve the management's production.
- (iii) Circumstances of corporate planning deficiencies, organization's structured defects, ineffective management control system etc. warrants the necessity of management audit.
- (iv) In the circumstances of acquisition of another business entity, the acquiring organization needs to evaluate financial aspects, technical aspects and management aspects and analysis of these aspects takes the form of management audit.
- (v) Society at large likes to be assured that the top and middle level management discharge their functions efficiently and to the best advantage to the society, the management audit satisfy the different interest of groups like customers, employees, citizens, government etc. of the society and also guide the management in the application of scientific methods of business management for social well being.
- (vi) The statutory financial audit is generally annual and concerned with the past without having any forward approach. Statutory financial audit and internal audit along with statutory cost audit are essentially legalistic in terms of time given for its completion and nature of certification fails to provide the insight to the management in regard to unsuitability of structure to meet the entity's needs, poor leadership, inability to make decisions, poor vision and the enlightened managers realizes this fact and feels the need of management audit to identify the problems and guidance to overcome them.
- (vii) Foreign collaborators, while investing in other organizations feel the necessity of management audit to ensure that the funds invested are to be used properly for growth and expansion.
- (viii) Financial institutions conduct the management audit, while participating in equities of a company to avoid possible losses arising from inefficient management.
- (ix) Company itself feels the need of management audit to assess its managers' performances and link an incentive system to the results of such assessment.
- (x) While advancing loans, banks like to get the management audit conducted.

(C) Scope of Management Audit

The scope of management audit can be as broad as the management process itself. It is concerned with the whole field of activities of a business concern from top to bottom of a management hierarchy. Management audit concerns with the appraisal of management policies, methods and performance, it includes review and appraisal of an organization to determine 1) Better means of control. 2) Greater improved methods. 3) More efficient operations. 4) Greater use of human and physical facilities and 5) Waste and deficiencies.

(D) Management Audit Process

Fundamentally the activities to be undertaken by management auditor in its review of material management, production management, industrial engineering management, sales management, financial management, general administration etc. include-

- (i) Collection and analysis of relevant statistics and reports used by the management.
- (ii) Establishment of priorities for various functional activities to be reviewed.
- (iii) Interviews and meetings with the senior, middle and supervisory management levels in order to ascertain
 - 1) How plans are developed. 2) How resources are controlled and 3) How performances are evaluated.

Who can conduct the management audit?

The management audit can be conducted by –

- (A) Company Talent- Which may include-
 - (1) An administrative staff.
 - (2) An audit committee.
 - (3) An officer on special duty. These personnel have sufficient knowledge of operations and talent necessary for the study, have no vested interest and are acceptable to other persons responsible for the area.
- (B) Outside Management Consultants- Who may be Chartered Accountants, Cost Accountants or Management Consultants having no vested interest in the company management, having no loyalty to any individual in the organization, having an impartial and objective approach, having wide range of specialties, have already developed the skill to carry on management audit.



- (C) Company Talent as well as Management Consultants- Considering the prevailing circumstances in a company a combination of company talent and outside management consultants would be a best team to conduct the management audit. The advantages of each compliment the other.

Whoever maybe appointed as management auditor, should possess the following qualities-

- (i) Ability to understand the problems of the business.
- (ii) General understanding as to nature and objects of the organization.
- (iii) Expert knowledge of the principles of delegation of authority, management by objectives, management by exception, management control, budgetary control, internal control, flow charts, use of computers etc.
- (iv) Sufficient knowledge and experience in preparing different reports for presentation to the different levels of management including top management.
- (v) Background of engineering, costing, statistics, management accounting, financial accounting, industrial psychology, managerial economics etc.
- (vi) General understanding of different laws and regulations like company laws, tax laws, etc.
- (vii) Tactfulness, perseverance, pleasing & dynamic personality.

(E) Advantages of Management Audit-

- (i) The company's personnel know the organizational policies, plans, personnel operations, personalities and working relationships, the political climate, the functional importance, and some of the problems themselves.
- (ii) The audit team need not spend an unduly long time for familiarizing themselves with the background information for study.
- (iii) It may be easier to get the support of the higher management, because such audit in the form of self-appraisal apparently involves no extra cost.
- (iv) The acceptance of the findings may be comparatively easier because the concerned personnel may readily accept the recommendations from the internal management audit team (consisting of co-workers) than from the external management auditors (or consultants).
- (v) The implementation of the new method of operation or organizational arrangement may be easier because the personnel who designed and advised it are on the premises. The constant co-operation necessary in the implementation phase are greatly facilitated.
- (vi) The experience and expertise gained by the company personnel in the conduct of management by self-appraisal could be gainfully utilized for subsequent audits.

(F) Limitation of Management Audit

- (i) The company personnel possess experience limited only to their organization. The company might have faced difficulties and constraints due to limited experience of the company personnel.
- (ii) They are more likely to take facts for granted and may not probe into the details to unearth problems.
- (iii) There may be a tendency to suppress unfavorable facts relating to some of the fellow personnel.
- (iv) The company may not have the talent necessary to conduct such management audit involving complicated studies.
- (v) It may not be possible for the company to spare personnel for the studies as these may take long time.
- (vi) It may be possible, due to conflicting interests that the audit work may be prolonged and as a result, the action on findings and recommendations may be delayed.
- (vii) The vested interests of the operational executives may prevent the management audit team from being objective.
- (viii) In a management audit scheme, the areas of investigation should fruitfully cover the entire management system, and so the situation demands the audit team to complete the studies under a time constraint- which may result in not covering some of the important appraisal areas.



QUESTION BANK - AUDITING

AUDITING BASICS - I

1. State with reasons, whether following statements are true or false :
 - (i) The concept of evidence is fundamental to all auditing situations as an auditor basically seeks to obtain sufficient appropriate evidence to form his opinion.
 - (ii) In all auditing situations, the only evidence available to the auditor is books of accounts and vouchers.
 - (iii) Not only statutory provisions but also technology and economic changes have influenced auditing to a great extent.
 - (iv) The decisions given by Hon. Courts in different cases do not affect the Generally Accepted Accounting and Auditing Practices and Standards.
 - (v) Auditing is generally associated with only accounting and financial records.
 - (vi) The scope of audit depends upon the nature of appointment.
 - (vii) The statutory audit provides the best means of enhancing the credibility of the accounts.
 - (viii) Auditor cannot gather sufficient appropriate audit evidence without performance of compliance and substantive tests.
 - (ix) Inspection and observation are not only the ways to obtain audit evidence.
 - (x) US-GAAP are not different than that of INDIA-GAAP.
 - (xi) Percentage test and past trends are the only criteria to establish the materiality of an item in financial statements.
 - (xii) The risk that the auditor gives an inappropriate audit opinion when the financial statements are materially misstated is called as an "audit risk".
2. What is Auditing? Explain the evolution on auditing.
3. Define "audit". What are the factors which drastically changed the present day auditing practice and auditor's responsibilities?
4. Write short notes on :
 - (a) Nature of auditing
 - (b) Change in scope of auditing
 - (c) Compliance Procedure
 - (d) Substantive Procedure
5. What is audit evidence? Explain the different types of audit evidence and different methods of obtaining them.
6. "Audit Technique is the device available to the auditor for obtaining competent evidential matter". Explain.
7. Write short notes on:
 - (a) Audit procedure
 - (b) Audit practices
 - (c) IFRS
 - (d) GAAS
 - (e) Concept of materiality in auditing
 - (f) Materiality and Audit Risk
8. "Audit practices demands the thorough knowledge of different legal provisions and different pronouncements"- Discuss.
9. Explain the important contents of US-GAAP.
10. Explain the important contents of INDIA-GAAP.



AUDITING BASICS - II

1. State with reasons, whether following statements are true or false :
 - (i) Items in the profit and loss account are verified from the ledger balances and this is sufficient to verify the correctness of Profit or Loss.
 - (ii) Comparing the voucher with the transaction recorded in the book of original entry is called as vouching.
 - (iii) While verifying the Sales appearing in the Profit and Loss Account, it is important that auditor, first of all should carefully verify the effectiveness of existing internal check system.
 - (iv) To verify the excisable value and calculation of duty the auditor checks the Daily Stock Account.
 - (v) Only the vouching to ascertain the arithmetical accuracy is not enough.
 - (vi) When proper purchase order, voucher, tenders etc., are available then auditor should not waste his time in checking concerned board resolution while verifying Plant and Machinery purchase.
 - (vii) Auditor is not required to get the inventory valuation certified by the company's management; he himself is qualified to ascertain the value.
 - (viii) Auditor is a watchdog and not a bloodhound.
 - (ix) Reserve not appearing on the Balance Sheet is a Secret Reserve and an auditor is not supposed to verify it.
 - (x) Section 210A of the Companies Act, deals with the constitution of National Advisory Committee on Accounting Standards.
 - (xi) All members of Accounting Standard Committee are the members of the Institute of Chartered Accountants of India.
 - (xii) The form of Balance Sheet given in Schedule VI of the Companies Act does not apply to the Insurance Companies, Banking companies and Electricity Companies.
 - (xiii) Auditor opting for the statistical sampling makes a big mistake.
 - (xiv) Auditor should not depend on the results derived from Ratio Analysis as the ratios are offspring of the "Statistics", which is not a perfect science.
 - (xv) Auditor, for proper reporting, avail of the Inter Firm as well as Intra firm comparison.
2. How would you verify the following items –
 - (i) Sales
 - (ii) Wages
 - (iii) Retirement benefits
 - (iv) Excise Duty
 - (v) Commission Received
3. How would you verify the following items –
 - (i) Plant and Machinery
 - (ii) Goodwill
 - (iii) Investments
 - (iv) Sundry Debtors
 - (v) Stock in Trade
4. Throw light on any of the following Two Case-Laws-
 - (i) Kingston Cotton Mill Co. Ltd., (C1896) (2CH 729)
 - (ii) Deputy Secretary, Ministry of Home Affairs Vs. S.N. Das Gupta
 - (iii) Irish Woolen Co. Ltd., Vs. Tyson and Other (1900)



5. What do you mean by the Disclosure of Accounting Policies and Practice – Discuss in brief.
6. Write Short Notes on –
 - (i) Expenditure during the period of construction
 - (ii) Adjustments for previous year
 - (iii) Books of Accounts to be kept by companies
7. What is “Statistical Sampling”? What are the methods of Statistical Sampling to be used in auditing and explain how the results of sampling are evaluated?
8. **P LTD.**

BALANCE SHEET AS ON 31.03.2010

LIABILITIES		ASSETS	
Equity Share Capital	2,00,000	Goodwill	1,20,000
Capital Reserve	40,000	Fixed Assets	2,80,000
8% Loan on Mortgage	1,60,000	Stock	60,000
Trade Creditors	80,000	Debtors	60,000
Bank Overdraft	20,000	Investments	20,000
Taxation – current	20,000	Cash in Hand	60,000
Profit and Loss Account			
Profit after taxation and			
Interest	1,20,000		
Less, Transfer	(40,000)		
	80,000		
	6,00,000		6,00,000

You are required to calculate Ratios for Testing –

- (i) Liquidity or Short Term Solvency
 - (ii) Long term Solvency
 - (iii) Profitability
 - (iv) Capital Gearing
9. What are Trend Analysis, Inter firm comparison and Intra-firm comparison? How can these be made useful while carrying on an audit assignment.



COMPANIES ACT PROVISIONS RELATING TO AUDIT

1. Fill in the blanks :

- (a) A person is qualified to become a company auditor if he is _____ Chartered Accountant.
- (b) A person is not qualified to become a Company Auditor, if he is convicted _____ for any offence.
- (c) It is _____ who has right to appoint Company Auditor annually.
- (d) Casual Vacancy of any auditor can be filled by the _____
- (e) Auditor can be removed by the _____ of the Company.
- (f) Co. Auditor has a right to receive all notices to any _____ of the company.
- (g) Co. Auditor has a right of lien on _____
- (h) Auditor should report the share holders about the _____ and _____ State of Affairs of the company.
- (i) For guilty of negligence auditor has to _____ the loss sustained by others.
- (j) Signing false audit report is the _____ liability of Co. Auditor.
- (k) Falsification of books of accounts is the _____ liability of Co. Auditor.

2. State whether the following statements are True or False.

- (a) A firm shall be qualified to be the Co. Auditor if any of the Partner is practicing Chartered Accountant.
- (b) Miss Rosy, a Chartered accountant and member of the Institute of Chartered Accountants of England & Wales and holding certificate of practice too is fully qualified to be an auditor in a company in India.
- (c) A joint stock company of Practicing Chartered Accountants is qualified for appointment as an auditor of a company in India.
- (d) An auditor can audit any number of companies, beyond 20.
- (e) First auditor is always appointed by the Board of Directors of a company.
- (f) Auditor of a Govt. Company is appointed by the Central Govt. on the advice of the Comptroller & Auditor General of India.
- (g) First auditor can be removed by the first General meeting, though appointed by the Board of Directors.
- (h) Company Auditor has no right to obtain all the information & explanations needed at the time of the conduct of the audit.
- (i) Auditor can't take any legal or technical advice from outside expert but can give advice to auditee company.
- (j) Auditor is not supposed to report whether the company has maintained all required books of accounts.
- (k) Auditor shall sign the Audit report , prepared by him .
- (l) Nobody is allowed to practice as an Auditor unless he is a member of the ICAI & holds a Certificate of Practice.
- (m) Nobody is allowed to practice a Cost Audit, though is a member of the ICWAI & holds a Certificate of Practice.
- (n) Liability for misfeasance means liability for breach of trust.

3. Answer in one sentence only.

- (a) What is the professional qualification of Company Auditor?
- (b) Who can become a Cost Auditor of a company?
- (c) A person disqualified for any reason to be a Co. Auditor is also disqualified to be an auditor of which companies?
- (d) When Central Govt. appoints a Company Auditor?
- (e) Who can remove the Co. Auditor?



- (f) Give any two important rights of Co. Auditor.
 - (g) What is an important duty of Co. Auditor to shareholders of the co.?
 - (h) To whom the auditor performs his duty of signing an Audit Report?
 - (i) What is the duty of Co. Auditor in case of investigation?
 - (j) What is liability of a Co. Auditor in case of negligence of duty?
 - (k) What are the civil liabilities of a Co. Auditor under Companies Act 1956?
 - (l) What are the criminal liabilities of a Co. Auditor under Companies Act 1956?
 - (m) What is the liability of a Co. Auditor u/s 197 of the Indian Penal Code?
 - (n) What is the punishment for professional misconduct under the Chartered Accountants Act, 1949?
 - (o) What is the punishment for professional misconduct under the Cost & Works Accountants Act 1959?
4. Discuss "Liabilities of an Auditor" under the Companies Act 1956?
5. What are the duties of Company Auditor?
6. Write Short Notes.
- (a) Qualifications of Company Auditor.
 - (b) Disqualifications of Company Auditor.
 - (c) Appointment of a Company Auditor.
 - (d) Removal of a Company Auditor.
7. Mr A a practicing Chartered Accountant is attending to the tax matters of XYZ Ltd. And for that purpose has to regularly attend to the Company from 10.00 a.m. to 2.00 p.m on all working days . He is paid Rs 5000 p.m for the same. XYZ Ltd. intends to appoint Mr A. as it's auditor at the ensuing general meeting. Advice Mr A. giving reasons whether he can accept the appointment.
8. What Qualifications are required for being appointed as an auditor in the case of limited company, a partnership and a proprietary concern?
9. When does an auditor become disqualified for an appointment? Discuss.
10. Discuss the liability of an auditor of a limited company to third parties for his negligence?
11. Write Short Notes.
- (i) Liability of an Auditor for misfeasance under Companies Act.
 - (ii) Auditor's Liabilities for misstatement in the prospectus.
 - (iii) Duties of Company Auditor.
12. Briefly discuss the Auditor's liability to third parties in relation to issue of a prospectus.
13. State the Provisions of the Companies Act 1956 with regard to the appointment of an Auditor.
14. Discuss the rights, duties & liabilities of the auditor of a company.
15. Discuss the statutory powers & duties of a company auditor.
16. What qualifications are necessary for the auditor of a Public Limited Company in India? Can the following be appointed as auditor of Limited Co.?
- (a) Mrs. X
 - (b) A partner of the Director of the company.
 - (c) A person of unsound mind.
 - (d) Mr. Y, who owes Rs. 500 to the company.
 - (e) A firm of which the Secretary of the Company is a member.



17. Who can be and who can't be appointed auditor of a company? Who can dismiss an auditor & how?

18. Fill in the Blanks.

- (i) Audit report gives _____ and _____ information.
- (ii) Audit report shall contain an expression of opinion regarding _____
- (iii) Audit report is the _____ product of the auditing.
- (iv) Audit report gives the auditors _____ on the accounts of record of the company.
- (v) Auditor should state in his report whether he has _____ all the information for his audit.
- (vi) Opinion in the audit report may be a) un-qualified b) qualified c) adverse
- (vii) Auditor should not give the certificate on his _____
- (viii) Auditor should address the certificate to _____
- (ix) Audit certificate is a written _____ of the accuracy of the information stated there in.

19. State whether following statements are true or false.

- (i) Audit Report is addressed to the persons who are already in possession of the full facts of the subject matter of the report.
- (ii) Audit report is not a medium of expressing auditors' opinion.
- (iii) Audit report doesn't reflect the work done by the auditor.
- (iv) Audit report mentions whether Balance Sheet & Profit & Loss Account attached there to gives a true & fair view.
- (v) The opinion stating that the auditor does not agree with the true & fair state of affairs exhibited by the final accounts is called as a "Disclaimer" opinion.
- (vi) Report with certain reservations is called as a qualified audit report.
- (vii) Auditor should clearly state his limitation in the certificate.
- (viii) Auditor is not expected to indicate the extent to which he has relied upon a technical expert, in the certificate.
- (ix) Auditor guarantees absolute correctness of the figures in the certificate.

20. (A) Answer in One sentence only.

- (i) What is an Audit report?
- (ii) What is Audit certificate?
- (iii) List down the contents of Audit Report?
- (iv) State the different opinions either of which is included in Audit Report.
- (v) What is qualified Audit report?
- (vi) What do you mean by an unqualified Audit report?
- (vii) To whom Audit certificate is addressed ?
- (viii) To whom Audit report is addressed ?
- (ix) Whether Audit Report or Audit certificate may provide suggestions for improvements?

(B) Describe Clean and Qualified Audit Report.

21. Write Short Notes.

- (i) Contents of Audit Report
- (ii) Qualified Report.

22. When should an auditor make a disclaimer of opinion in his audit report?

23. The Company had set-up a factory on coastal land. In view of the corrosive climate, the machine life was reducing faster and, therefore, it wanted to charge a higher rate of depreciation.
What should be the opinion of the auditor?

24. What are the circumstances under which an auditor cannot issue an opinion other than a qualified opinion?



25. What aspects should an Auditor consider in expressing a qualified opinion in his report.
26. Under what circumstances is a disclaimer of opinion issued by an auditor?
27. What are Audit Reports and Audit Certificates? Discuss their importance?
28. Draft a qualified audit report, inserting three qualifications therein.
29. Draft an unqualified audit report.
30. State whether following statement are true or false
 - (1) In companies other than Banking and Insurance, the Joint Auditors are appointed as per the regulations of those Companies.
 - (2) Branch Audit should be conducted by the Company Auditor.
 - (3) Branch Auditor need not be a Chartered Accountant.
 - (4) Branch Auditor, if appointed separately, submit his report to the H.O. only.
 - (5) No Government has any power to direct any special audit.
 - (6) Internal Auditor should be appointed by the Board of Directors.
 - (7) Corporate governance is nothing but only a paper work.
31. What do you mean by Joint Audit? Explain the advantage and disadvantage of Joint Audit.
32. What are the Power, Duties and Rights of a Company Auditor towards Branch Accounts and Branch Auditors.
33. What are the provision of the Income Tax Act, 1961 regarding Audit of Accounts of certain person carrying on business or profession.
34. Explain the interface between Statutory Auditor and Internal Auditor.
35. Draft the specimen of Auditor's certificate on company's compliance of corporate governance as per the clause 49 of The Listing Agreement.



REVIEW AND AUDIT OF INTERNAL CONTROL SYSTEM

1. State with reasons whether the following statement are TRUE or FALSE.
 - (i) Internal Audit is entrusted to the employees of the organization.
 - (ii) When there is a Statutory Audit, introduction of Internal Audit is not necessary at all.
 - (iii) Evaluation of the performance is called as operational audit.
 - (iv) To examine whether the transactions have been done in conformity with the established standard is nothing but the Proprietary Audit.
 - (v) Certified statements showing turnover of the company fall under the category of the compliance audit
 - (vi) The Companies (Auditor's Report) order 2003 applies to all companies.
 - (vii) The CARO extend the scope of audit even further than that of traditional approach.
 - (viii) To be successful, the internal audit department must have adequate management support.
 - (ix) Audit to internal audit function is considered necessary.
 - (x) Statistical sampling in Auditing relieves an auditor from the load of work but not from the risk.
 - (xi) Internal Audit is similar to that of internal control.
 - (xii) Internal check is necessary only to comply with the provisions of the CARO.
 - (xiii) Audit Committee is only the luxury to the company.
 - (xiv) Detection of frauds is the duty of the Statutory Auditor and not necessarily that of an internal auditor.
2. What is an Internal Audit ? Explain the necessity and scope of Internal Audit.
3. Write short notes.
 - (i) Financial Audit And Operational Audit.
 - (ii) Efficiency Audit and Propriety Audit.
 - (iii) Voucher Audit and Compliance Audit
 - (iv) Audit Programme and Audit Note Book
4. What do you mean by CARO? Explain what is expected under the CARO regarding —
 - (a) Inventory
 - (b) Internal Audit
 - (c) Internal Control
 - (d) Deposit of Statutory Dues.
 - (e) Frauds
5. As an Internal Auditor, how would you examine the payment of wages and salaries.?
6. As an Internal Auditor, explain in detail the verification of Inventory Control System.
7. Write short notes :
 - (a) Flow chart
 - (b) Statistical sampling in Auditing
 - (c) Internal Auditor and Internal Control.
8. What is an Internal Audit ? Explain the constituents of field work of Internal Audit.
9. What do you mean by an Audit Report ? Explain the different techniques of effective reporting.
10. Define Internal Audit and explain in detail the role of Internal Auditor in investigation of frauds.
11. What is Audit Committee, what is the scope and function of audit committee?



INFORMATION SYSTEM AUDIT AND MANAGEMENT AUDIT

1. State whether following statements are true or false :
 - a. When information system audit is an information technology audit, the auditor is required to have the detailed knowledge of accounting rather than information system.
 - b. Information system audit is the audit of the accounting controls.
 - c. At the time of preparing information system audit program, auditor must understand the system.
 - d. Audit in the case of Electronic Data Exchange is a difficult task.
 - e. Auditor should test check controls established to reduce the risk associated with commerce transactions.
2. What is information system audit? Explain the audit procedure in system audit to determine the material losses.
3. Define computer information system audit and explain the nature of risks and internal control characteristics in CIS environment.
4. Write short notes on –
 - (a) Types of IT audit
 - (b) System audit
 - (c) Computer audit
 - (d) Input controls
 - (e) Processing controls
5. What is computer assisted audit technique? Explain the different computer assisted techniques available.
6. What is CIS audit? Explain its application in case of E-commerce.
7. Explain :
 - (a) Audit in online system environment.
 - (b) Audit in case of environment of personal computer.
8. Define management audit. Discuss need of Management Audit.
9. What are the advantages and limitation of Management Audit?