GUIDELINE ANSWERS

PROFESSIONAL PROGRAMME

DECEMBER 2016

MODULE 3

THE INSTITUTE OF
Company Secretaries of India
IN PURSUIT OF PROFESSIONAL EXCELLENCE
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These answers have been written by competent persons and the Institute hopes that the **GUIDELINE ANSWERS** will assist the students in preparing for the Institute's examinations. It is, however, to be noted that the answers are to be treated as model answers and not as exhaustive and the Institute is not in any way responsible for the correctness or otherwise of the answers compiled and published herein.

In answers to the questions based on case study, the students may write any other alternative answer with valid reasoning.

The Guideline Answers contain information based on the Laws/Rules relevant for the Session. Students are expected to be well versed with the amendments in the Laws/Rules made upto **six** months prior to the date of examination.

C O N T E N T S

NOTE : Guideline Answers of the last Sessions may require updation in the light of changes and references given below :

PROFESSIONAL PROGRAMME

UPDATING SLIP

ADVANCED TAX LAWS AND PRACTICE

MODULE – 3 – PAPER 1

Examination Session	*Question No.*	*Updations required in the answers*
All Previous Sessions	—	The Income Tax, Service Tax, Sales Tax, Central Excise and Customs Laws are subject to changes by the Annual Finance Acts. In order to update all the answers, the students are advised to refer to the latest law keeping in mind the following amendments for June 2017 examination. (i) For Direct taxes, Finance Act, 2016 is applicable. (ii) Applicable Assessment year is 2017-18 (previous year 2016-17). (iii) Wealth Tax Act, 1957 has been abolished w.e.f. 1st April, 2016. The questions from the same will not be asked in examination from December 2015 session onwards. (iv) For Indirect taxes, all changes made by the Finance Act, 2016 are also applicable. (v) Students are also required to update themselves on all the relevant Circulars, Clarifications, Notifications, issued by CBDT / CBEC/ Central Government etc. which became effective, on or before six months prior to the date of the respective examination. The questions based on case laws, in conflict with the latest law be treated as of academic interest only.

UPDATING SLIP

DRAFTING, APPEARANCES AND PLEADINGS

MODULE – 3 – PAPER 2

Examination Session	*Question No.*	*Updations required in the answers*
All Previous Sessions	—	Provisions of Companies Act, 2013.

UPDATING SLIP

BANKING LAW AND PRACTICE

MODULE – 3 – ELECTIVE PAPER 9.1

Examination Session	*Question No.*	*Updations required in the answers*
All Previous Sessions	—	All relevant amendment pertaining to Banking Laws and Notification/Circulars issued thereunder upto 6 months prior to the date of examination.

UPDATING SLIP

CAPITAL, COMMODITY AND MONEY MARKET

MODULE – 3 – ELECTIVE PAPER 9.2

Examination Session	*Question No.*	*Updations required in the answers*
All Previous Sessions	—	In accordance amended Regulations covering Capital Commodity and Money Market. SEBI (Listing Obligations and Disclosures Requirements) Regulations, 2015. All answers pertaining to listing of securities and corporate governance to be updated accordingly. SEBI (Prohibition of Insider Trading) Regulations, 2015. All answers pertaining to price sensitive information, insider trading to be updated accordingly. Master Circulars issued by RBI from time to time.

UPDATING SLIP

INSURANCE LAW AND PRACTICE

MODULE – 3 – ELECTIVE PAPER 9.3

Examination Session	*Question No.*	*Updations required in the answers*
All Previous Sessions	—	All notifications issued by Insurance Regulatory and Development Authority of India (IRDA).

UPDATING SLIP

INTELLECTUAL PROPERTY RIGHTS — LAW AND PRACTICE

MODULE – 3 – ELECTIVE PAPER 9.4

Examination Session	*Question No.*	*Updations required in the answers*
All Previous Sessions	—	In accordance with revised laws, rules under TRIPS, and World Intellectual Property Organization (WIPO) and National Intellectual Property Rights Policy.

UPDATING SLIP

INTERNATIONAL BUSINESS - LAWS AND PRACTICES

MODULE – 3 – ELECTIVE PAPER 9.5

Examination Session	*Question No.*	*Updations required in the answers*
All Previous Sessions	—	In accordance with revised laws and rules under WTO, IMF, UNCTAD, etc, if any.

ADVANCED TAX LAWS AND PRACTICE

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *1. Answer ALL Questions.*

2. All the references to sections mentioned in Part - A of the Question Paper relate to the Income-tax Act, 1961 and relevant Assessment Year 2016-17, unless stated otherwise.

PART A

Question 1

(a) Global Ltd. is a widely-held company engaged in power generation in Assam. At present, the company is having a capital of ₹10 crore in fully paid equity shares. The company is considering a proposal to increase its power generation capacity which will require ₹5 crore. The additional capital required can be raised either by issue of fully paid equity shares or by issue of 10% debentures. Directors of the company want to raise the funds through equity shares as the company can have fully owned capital. Will you accept the proposal at 20% rate of return (pre-tax) and 30% rate of tax ? Give reasons. in support of your answer. (5 marks)

(b) Karan purchased a plot in 1987-88 for ₹2,10,000. He sold the plot on 7th February, 2016 for ₹24,00,000 (stamp duty value ₹25,40,000). He paid a brokerage of 5% on selling price to a person who arranged for the sale. Out of the sale proceeds of the plot, he invested ₹5,00,000 in NHAI Bonds on 31st March, 2016 and ₹3,00,000 in bonds of Rural Electrification Corporation Ltd. on 1st September, 2016.

Compute the taxable capital gains of Karan, if the cost inflation index (CII) for 1987-88 was 150 and for 2015-16 is 1081. (5 marks)

(c) Brisk Ltd. incurred ₹52.75 lakh during the period April, 2015 to June, 2015 on advertisement, professional fees, administration cost, etc. for the purpose of public issue of ₹555 crore in July, 2015 and had, therefore, accounted all such expenses under the head 'share issue expenses', However, the clearance for the public issue was not given by SEBI. The company in its return of income filed for the year ended 31st March, 2016 had claimed such expenses as revenue expenses which were disallowed by the Assessing Officer.

The company seeks your opinion. Advise. (5 marks)

Answer 1(a)

Computation of Expected Rate of Return on Capital Employed

Particulars	*Amount in Rs.*	
	(Proposal I) Issue of Equity Shares	*(Proposal II) Issue of 10% Debenture*
Equity Share Capital	15,00,00,000	10,00,00,000
10% Debenture	-	5,00,00,000

Particulars	*Amount in Rs.*	
	(Proposal I) Issue of Equity Shares	*(Proposal II) Issue of 10% Debenture*
Total Capital Employed	15,00,00,000	15,00,00,000
PBIT (Expected Rate of Return @ 20% of total Capital employed)	3,00,00,000	3,00,00,000
Less: Interest on Debenture @10%	-	(50,00,000)
Profit Before Tax	3,00,00,000	2,50,00,000
Less : Tax @ 30% on PBT	(90,00,000)	(75,00,000)
Net Profit After Tax	2,10,00,000	1,75,00,000
Expected Rate of Return to Share Holders	14.00%	17.50%

Conclusion : The proposal of deriving additional capital by issuing fully paid up equity shares is not acceptable as it will give lesser rate of return to share holders in future. Therefore, it is beneficial to raise the additional funds through the issue of 10% Debentures as it will increase the rate of return to shareholders from 14% to 17.50 %.

Answer 1(b)

Computation of Capital Gain

Particulars	Amount (in Rs.)
Seles Consideration of Plot (Stamp duty value u/s 50C has been considered as full value of consideration as the actual sale value is less than the stamp duty value)	25,40,000
Less : Brokerage paid on sale of plot (5% of Rs. 24,00,000)	(1,20,000)
Less : Indexed Cost of Acquisition (Rs. 2,10,000 *1081/150)	(15,13,400)
Long Term Capital Gain (LTCG)	9,06,600
Less : Exemption u/s 54EC (Purchase of NHAI Bond)	5,00,000
Net Taxable LTCG	4,06,600

Note : Investment in Rural Electrification Corporation Ltd. is not eligible for exemption as it was made after six months from the date of transfer.

Answer 1(c)

The assessee company (Brisk Ltd.) had claimed expenditure of Rs. 52.75 lakhs as “share issue expenses” being incurred “wholly & exclusively for business purposes”. It further contends that incurring of such expenses did not result in increase in the share capital of Company for the reasons beyond their control and therefore claimed as revenue expenditure.

The contention of the assessing officer is that such expenses are capital expenditure because the company had taken steps to go in for a public issue and consequently

incurred such expenses. Despite the fact that the proposed issue could not materialize due to restrictive order by SEBI does not make such expense as revenue expense. The important issue is that such expenses were incurred wholly and exclusively for the purpose of expansion of Capital base of the company and thus the expenditure incurred would not lose its character as capital expenditure as the assessee had admittedly took steps to go for public issue and after incurring expenditure, just before the public issue, by reason of the orders from the SEBI, the assessee could not go in for public issue.

Therefore the expenses of Rs. 52.75 lakhs incurred by Brisk Ltd. hence be disallowed being "capital expenses" and action taken by the Assessing Officer is lawful and correct. [*This view was upheld by Madras High Court in the case of Mascon Technical Services Ltd. v/s CIT (2013) 358 ITR 545*]

Attempt all parts of either Q. No. 2 or Q. No. 2A

Question 2

(a) Explain in brief the treatment as to the taxability and/or allowability, in the context of provisions contained under the Income-tax Act, 1961 for the assessment year 2016-17, in the following cases :

(i) Aroma Ltd., an investment company, received dividend of ₹3,00,000 on equity shares from listed domestic companies. It paid interest of ₹2,00,000 on the borrowed funds utilised for making investment in such shares of these companies.

(ii) Chetan Ltd. did not have any active business carried on by it during the previous year ended on 31st March, 2016 and had incurred capital expenditure on scientific research amounting to ₹2,00,000 related to its subsidiary company. (5 marks)

(b) Distinguish between 'tax planning' and 'tax avoidance'. (5 marks)

(c) When can uncontrolled transactions be taken as comparable to international transactions ? Which data can be used for the comparability of an uncontrolled transaction with an international transaction ? (5 marks)

OR (Alternate question to Q.No. 2)

Question 2A

(i) Mohan owns a house located in Varanasi. The construction of the house was completed in July, 2011. One-fourth floor area of the house is utilised by him for his own residence. He is running his own clinic in another one-fourth floor area of the house. The remaining floor area is let-out for residential purposes on a monthly rent of ₹8,000.

The let-out portion of the house remained vacant for two months during the previous year 2015-16. Other details of the entire house are as under :

	₹
Standard rent	*1,60,000*
Municipal valuation	*1,40,000*
Municipal tax paid by Mohan	*20,000*

Interest payable on loan taken for construction of the house	*60,000*
Repairs and maintenance	*8,000*
Insurance	*4,000*

Compute income from house property of Mohan for the assessment year 2016-17. (5 marks)

(ii) Arvind, a textile merchant and resident Indian is doing business in India and abroad. During the previous year 2015-16, he disclosed the following information:

	₹
Income from business in India	*27,00,000*
Income from business in Country-A with which India does not have agreement for avoidance of double taxation	*15,00,000*
Income-tax levied by government in Country-A	*5,00,000*
Loss from business in Country-B with which also India does not have agreement for avoidance of double taxation	*(4,00,000)*
Contribution to public provident fund	*1,50,000*
Payment of life insurance premium on the life of his father and mother	*20,000*

Compute the tax liability of Arvind for the assessment year 2016-17. *(5 marks)*

(iii) Nandita Traders, engaged in manufacturing activity, was in receipt of sales-tax subsidy of ₹5 lakh from State Government as its manufacturing unit was located in a backward area. The subsidy is related to the sales of its products and was payable only after the commencement of production. Nandita Traders claimed that the subsidy so received is in the nature of capital receipt and hence, cannot be taken as chargeable to tax for the assessment year 2016-17. How will you deal with the situation in the context of provisions of the Income-tax Act, 1961? *(5 marks)*

Answer 2(a)

(i) The dividend income of Rs. 3,00,000 earned by Aroma Ltd. on equity shares held as investment in domestic companies is exempt under the provisions of section 10(34) of the Income tax-Act, 1961.

Further, as per section 14A of the Income-tax Act, 1961, no expenditure is allowable in respect of income which does not form a part of total income or which is an exempt income. The interest paid of Rs. 2,00,000 on borrowed capital is an expenditure incurred in respect of share purchased for investment. Since the dividend income received on shares is exempt and does not form a part of total income of Aroma Ltd., the interest expenditure of Rs. 2,00,000 incurred by Aroma Ltd. is not allowable as deduction in the AY 2016-17.

(ii) As per section 35(1)(iv) of the Income Tax Act 1961, deduction in respect of capital expenditure on scientific research would be admissible under the provisions of section 35(2) only, if, the scientific research relates to the business carried on by the assessee.

In the given case, Chetan Ltd. did not have any active business carried on by it to which said scientific research related to. The capital expenditure incurred by Chetan Ltd. related to its subsidiary company. Accordingly, Chetan Ltd, had not incurred any expenditure on scientific research relating to its business and is not eligible for deduction under the provision of section 35(1)(iv) and therefore the expenses is not allowable as deduction.

Answer 2(b)

Sr. No.	*Tax Planning*	*Tax Avoidance*
1.	Tax planning is an act within the four corners of the tax laws. It is a mean to avail the benefits legally permissible under the Act.	It complies with the legal language of the law but not the spirit of the law.
2.	Tax planning is a permissible legal right which enables the tax payer to maximize his return net of taxes.	It refers to reducing the tax liability by finding out loopholes in the law.
3.	Tax planning has judicial approval.	The concept can be considered heinous to tax evasion. Government brings amendments to curb such practices and to plug the loop holes.
4.	It does not result in levy of penalty and prosecution as it is within the language and spirit of law.	It may result in disregarding the transaction done to avoid tax and may / may not result in penalties and prosecution against the person engaged in it.
5.	An Individual made investment in PPF to claim deduction under section 80C is an example of tax planning.	An assets transferred by one person to another person without consideration / without adequate consideration may be treated an example of Tax Avoidance.

Answer 2(c)

As per rule 10B(3), uncontrolled transaction can be taken as comparable to international transaction only if-

(a) none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market; or

(b) Reasonably accurate adjustments can be made to eliminate the material effects of such difference.

If the differences are material and the adjustments cannot be made, the transaction cannot be taken as comparable transaction, then such transaction shall be ignored. Further, as far as possible the internal comparable (i.e. transactions entered into by the associated enterprise with unrelated party) should be selected as these will provide more reliable and accurate data as compared to external comparable data i.e. (transaction with third parties).

As per rule 10B(4), the data to be used in analyzing the comparability of an uncontrolled transaction with an international transaction shall be the data relating to the financial year in which the international transaction has been entered into.

However, data relating to a period not being more than 2 years prior to such financial year may also be considered if such data reveals facts which could have an influence on the determination of transfer prices in relation to the transactions being compared.

Answer 2A(i)

Computation of Income from House Property of Mohan for the AY 2016-17

Particulars	*Amount (in Rs.)*	
Annual Value of ¼ portion used for his own profession	Nil	
Annual Value of ¼ portion used for his own residence	Nil	
Less : Municipal Taxes	Nil	
Net Annual Value	Nil	
Less : Interest on Borrowing (1/4 * Rs. 60000)	(15,000)	
Loss from house property (Self Occupied)		(15000)
Gross Annual Value of let-out portion (Rs. 80,000 * 10)	80,000	
(a) Expected Rent = Fair Rent or Municipal Value which ever is higher subject to Standard Rent i.e. Rs. 1,40,000 / 2 = 70,000		
(b) Gross Annual Value = Expected Rent or Actual Rent whichever is higher i.e. Rs. 70,000 or (Rs. 8,000*10) = Rs. 80,000		
Less : Municipal Tax (Rs. 20,000 * ½)	(10,000)	
Net Annual Value	70,000	
Less : Standard Deduction (Section 24b) (Rs. 70,000 *30%)	(21,000)	
Less : Interest on Borrowing (Rs. 60,000 * ½)	(30,000)	
Income from let out house property		19,000
Income under the head house property		**4,000**

Note : Expenses on Repair and Maintenance and Insurance would not be allowed as deduction in computing the income under the head house property.

Answer 2A(ii)

Computation of Taxable Income &Tax Liability of Arvind for the AY 2016-17

Computation of Taxable Income and Tax Liability	*Amount (In Rs.)*	*Amount (In Rs.)*
Business Income earned from India	27,00,000	
Business Income earned from Country A	15,00,000	
Business Income earned from Country B	(4,00,000)	
Gross Total Income	38,00,000	
Less : Deduction under Chapter VI-A	(1,50,000)	
Total Income		36,50,000
Tax Liability On first Rs. 2,50,000 - NIL		
Rs. 2,50,001 - Rs. 5,00,000 - 10%		25,000
Rs. 5,00,000 - Rs. 10,00,000 - 20%		1,00,000
Balance @ 30% (Rs. 26,50,000 * 30%)		7,95,000
Total Tax (excluding EC & SHEC)		9,20,000
Education Cess & SHEC @ 3%		27,600
Total Tax		9,47,600
Relief under section 91 (Note 1)		(3,89,425)
Tax payable in India		5,58,175

Note 1

Computation of Relief under section 91 of the Income Tax Act, 1961

Average rate of Tax in India Rs. (9,47,600/36,50,000 * 100) = 25.9616 %	
Average rate of tax in foreign country (5,00,000/15,00,000*100) = 30%	
Doubly Taxed Income	15,00,000
Relief under section 91 (on Rs. 15,00,000 @25.96%) i.e. rate 25.9616 % or 30 % whichever is lower	3,89,425

Answer 2A(iii)

The Supreme Court in its judgment in the case of *Sahney Steel and Press Works Ltd.* v/s *CIT* (1997) 228 ITR 253 (SC) has held that the payment from public funds to assist the assessee in carrying on trade or business must be treated as revenue receipt. The subsidy granted to the assessee such as sales tax refund, power concession or refund of bills paid and exemption from payment of water charges are to be treated as revenue receipts chargeable to tax. It was held that the character of the subsidy in the

hands of the recipient will have to be determined having regard to the purpose of which the subsidy is given. If the monies are given for assisting the assessee in carrying out the business operations and the money is given only after and conditional upon commencement of production, the assistance must be treated as assistance for the purpose of the trade. Therefore on the facts of the case, the sales tax subsidy was nothing but supplementary trade receipts chargeable to tax in the hands of Nandita Traders in AY 2016-17. Moreover, the Income-tax Act, 1961 was amended by the Finance Act, 2015 to insert sub-clause (xviii) in section 2(24) to tax such receipts as "Income". The amended provisions are applicable from the assessment year 2016-17.

PART - B

Question 3

(a) Zebra Ltd. is engaged in the manufacture of various types of machines. It had supplied one machine to Tiger & Co. at a price of ₹17,00,000 (excluding taxes and duties).

Following additional amounts were charged from Tiger & Co. :

	₹
Expenses pertaining to installation and erection of the machine at the premises of Tiger & Co. (machine was permanently affixed to earth)	*50,000*
Packing charges	*8,000*
Design and engineering charges	*6,000*
Pre-delivery inspection charges (charged by Zebra Ltd.)	*2,000*
Bought out accessories supplied with machine	*8,000*

Tiger & Co. had supplied material worth 10,000 free of charge to Zebra Ltd. for being used in manufacturing of this machine.

You are required to work out the total amount of excise duty payable on the machine when the rate of excise duty is 12.5%. (5 marks)

(b) Rajan Textiles Ltd., a large scale industry in Mumbai, purchased a machine used for pollution control on 1st October, 2013 for a cum duty price of ₹9,00,000. Excise duty was levied at the rate of 12.5%. The machine was used upto 20th August, 2015 on which date it was sold for a transaction value of ₹6,00,000, excluding excise duty. The rate of excise duty on the date of sale was 12%. The machine was received in the factory on the date of purchase itself.

Calculate the CENVAT, credit allowable for the financial year 2013-14 and 2014-15 to Rajan Textiles Ltd. Also calculate the amount payable on reversal of credit due to sale of the machine in the financial year 2015-16. (5 marks)

(c) Nathan Ltd. gives a works contract to Samy Ltd. for a gross consideration of ₹12,00,000 (excluding all taxes). As per the terms of the contract all the materials and labour required for the contract are to be supplied by Samy Ltd. and Nathan

Ltd. accepted to supply certain other materials. Samy Ltd. provides the following particulars with regard to the works contract :

	₹
Fair market value of materials supplied by Nathan Ltd.	*2,50,000*
Actual amount charged by Nathan Ltd. for the materials including VAT	*1,50,000*
Excise duty paid on inputs used for the contract	*16,000*
Excise duty paid on capital goods purchased and used for the contract	*8,000*
Service tax paid on input services	*11,000*

If the rate of service tax is l4%, compute the service tax liability. *(5 marks)*

(d) Rohan is a trader selling raw materials to manufacturers for using the material to make finished products. He procures the material of his stock-in-trade from other States as well as from the local markets.

Following transactions pertain to a sale made by Rohan to a manufacturer for the month of March, 2016 :

	₹
Cost of materials procured from other States excluding central sales tax	*3,00,000*
Cost of materials purchased from local market (VAT not included)	*6,00,000*
Other expenditure including storage, transport, interest, loading, unloading, etc.	*94,000*

The goods are sold at 10% profit on cost of production. Calculate the invoice value charged by Rohan to the manufacturer by taking VAT rate to be 12.5% and central sales tax rate to be 2%. Also work out the amount of VAT payable by him. *(5 marks)*

(e) Zuhi Ltd. has imported a machine to be used for providing a taxable service. The assessable value of imported machine as approved by customs is ₹5,00,000. Customs duty @ 10% is payable. Further, if the machine is manufactured in India, excise duty @ 12% is leviable on such machine. Education cess and secondary and higher education cess are applicable as per prevailing rates. Special CVD @ 4% is also payable on such machine.

You are required to —

(i) Calculate the total customs duty payable on such machinery; and

(ii) Examine whether Zuhi Ltd. can avail CENVAT credit and if yes, how much CENVAT credit can be availed. *(5 marks)*

Answer 3(a)

Computation of Excise Duty payable on Machine by Zebra Ltd.

Particular	*Amount (in Rs.)*
Price of Machine (excluding taxes and duties)	17,00,000
Installation and Erection Charges (Note1)	-
Packing Charges (Note 2)	8,000
Design and engineering charges (Note 3)	6,000
Cost of Material (supplied free of charge by buyer) used in production of machine (Note 4)	10,000
Pre-Delivery inspection charges (Note 5)	2,000
Bought out accessories	-
Assessable Value	17,26,000
Excise Duty @12.5% on Assessable Value	2,15,750

Notes:

(1) Installation, erection and commissioning charges should be included only if such installation etc. results in a movable property, as in the present case, machine is permanently affixed to earth therefore such installation etc. does not result in emergence of movable property, hence not includible. (Circular No. 643/34/2002 CX dated 01.07.2002).

(2) Amount charged from buyer in relation to packaging (whether primary or secondary) will be included (Circular No. 354/81/2000 TRU dated 30.06.2000).

(3) As per Rule 6 of Valuation Rules, 2000, design and engineering charges will be included in computation of assessable value as such payment is 'in connection with sale'.

(4) Cost of material supplied free of charge by buyer will form a part of assessable value as it is additional consideration flowing from the buyer to seller (Explanation 1 to Rule 6 of the Central Excise Determination of Price of Excisable Goods) Rules 2000.

(5) Since, pre delivery inspection charges are charged by the manufacturer, the same is includible in the assessable value.

(6) Bought out accessories, supplied along with the machinery, assumed to be non essential, and thus not been included.

Answer 3(b)

When capital goods are removed after use, amount of cenvat credit reversible shall be calculated as per Rule 3(5A) of Cenvat Credit Rules, 2004 as below:

Computation of CENVAT Credit

Sr. No.	*Particular*	*Amount (in Rs.)*
A	Cum-duty Price of the Machine	9,00,000
	Rate of Excise Duty	12.50%
	Excise Duty Paid (Rs. 9,00,000 *12.50 / 112.50)	1,00,000
B	Cenvat Credit Allowable on the amount	
	For 2013-14 (50% in the first financial year)	50,000
	For 2014-15 (50% in the subsequent financial year)	50,000
C	Calculation of CENVAT Credit Repayable due to resale of Machine	
(i)	Cenvat Credit Availed	1,00,000
	Less : On First 50% (50,000 * 2.5%) *8	(10,000)
	Less : On Second 50% (50,000 * 2.5%) *6	(7,500)
		82,500
(ii)	Transaction Value of resale	6,00,000
	Rate of Excise duty on the date of sale	12%
	Excise Duty on resale (Rs. 6,00,000 * 12%)	72,000
	Reversible Cenvat Credit due to resale of assets is (i) or (ii) whichever is higher	82,500

Note : As per Rule 2A (ii) of Valuation Rules, 2006 when details of labour and other service charges are not available, value of services shall be computed under composition scheme at a fixed percentage of contract price.

Answer 3(c)

Computation of Service Tax Payable

Particular	*Amount (in Rs.)*
Gross Consideration (a)	12,00,000
FMV of materials supplied by contractee (b)	2,50,000
Less: Amount Charged by contractee (c)	(1,50,000)
Total Value of Contract (d=a+b-c)	13,00,000
Value of Service Portion (70%) i.e. Rs. 13,00,000 *70%	9,10,000
Service Tax @ 14%	1,27,400
Less : Input Tax Credit:	
Service Tax Paid Rs. 11,000	
Excise duty paid on capital goods @ 50% * 8,000 = 4,000	(15,000)
Net Service Tax Payable	1,12,400

Notes:

1. No CENVAT Credit is allowed on the Excise duty paid on input used for works contract.
2. It is presumed that the works contract is NOT original work. If it is taken as original work, it will be 40% of 13,00,000.
3. Only 50% of duty paid on capital goods has been taken as cenvat credit on the assumption that the works contract has been completed within first year of bringing in the capital goods.

Answer 3(d)

Computation of Invoice Value to a manufacturer under VAT

Particular	*Amount (in Rs.)*
Cost of Materials procured from other states excluding tax	3,00,000
Add : CST will be included in the Cost of inputs	6,000
Add : Cost of local Materials	6,00,000
Add : Other expenses	94,000
Total Cost of Production	10,00,000
Add : Profits 10% on cost of production	1,00,000
Sales Price	11,00,000
Output VAT @ 12.5% (Rs. 11,00,000 @12.5%)	1,37,500
Less : Input VAT credit (Rs. 6,00,000 *12.5%)	(75,000)
Net VAT Payable	62,500

Note : Since ITC is not available on CST, it becomes the part of cost of production.

Answer 3(e)

(i) Computation of Customs Duty Payable by Zuhi Ltd.

	Particulars	*Amount (In Rs.)*	*Duty (In Rs.)*
	Assessable Value	5,00,000	
	Basic Customs Duty @ 10% (a)	50,000	50,000
	Sub Total	5,50,000	
	Add : CVD @ 12% of Rs. 5,50,000) (b)	66,000	66,000
	Total	6,16,000	1,16,000
	EC + SHEC @ 3% (c)	3,480	3,480
	Total	619,480	1,19,480
	Add : Special CVD @4% on 619,480 (Rs. 5,00,000 + Rs. 50,000 + Rs. 66,000 + Rs. 3,480) (d)	24,779	24,779
	Total	6,44,259	1,44,259

(ii) As Zuhi Ltd. is a service provider, it can avail Cenvat Credit only for CVD of Rs. 66,000 and not of special CVD of Rs. 24,779

Attempt all parts of either Q.No. 4 or Q.No. 4A

Question 4

(a) Neon Ltd. classified one of the products manufactured by it as per the Central Excise Tariff Act, 1985 as a'nil'rate product. The excise department classified the same product under another heading attracting 11% duty as per Harmonised System of Nomenclature (HSN) for the purpose of classification of the impugned product. But, the entries in the HSN and the Central Excise Tariff Act, 1985 are not aligned. Give your opinion on this matter of classification with the help of a decided case law. (5 marks)

(b) While conducting search and seizure in the premises of Alpha Ltd., the officials recovered large quantity of chemicals. It was found that the chemicals were imported into India without any import license. After adjudication, penalty was imposed and the chemicals were confiscated. However, the Department gave an opportunity to the company to get back the goods after paying fine and duty at the prescribed rate. During the period, the Department notified the chemicals as exempted from customs duty. The assessee claimed the benefit of exemption notified.

Give your opinion whether the claim of Alpha Ltd. is tenable ? Discuss in the light of a relevant case law. (5 marks)

(c) Raj Sugars Ltd. is a manufacturer of sugar. The sugar manufactured by the company is sold to government for free supply and in the open market. The Government, to meet the market demand fluctuations, directed the sugar companies to maintain buffer stock. Also, the Government is giving subsidy to the sugar companies to meet out the storage, interest and insurance charges. Accordingly, Raj Sugars Ltd. received subsidy of Rs. 7,00,000. The Department contended that the subsidy earned by the company from the Government is an income earned from the service of storage and warehousing of goods and hence, taxable. Do you accept the contention of the Department ? Support your argument with a suitable case law. (5 marks)

OR (Alternate question to Q.No. 4)

Question 4A

(i) Nargis Agro Ltd., having a manufacturing unit situated in Jodhpur, made total clearances in the financial year 2014-15 of the total value of ₹525 lakh. The break-up of clearances so made is as under :

- *Clearances worth ₹100 lakh of certain non-excisable goods manufactured by it*
- *Clearances worth ₹75 lakh exempted under specified job work notification*
- *Exports worth ₹75 lakh (₹50 lakh to USA and ₹25 lakh to Nepal)*
- *Clearances worth ₹275 lakh of excisable goods in the normal course*

Explain briefly the treatment to be given for various items and work out whether the unit will be eligible for the benefit of exemption under Notification No. 8/ 2003-CE dated 1st March, 2003 as amended for the financial year 2015-16 *(5 marks)*

(ii) (a) Examine whether service tax is leviable in the context of provisions of the Finance Act, 1994 when services are provided in a vessel stationed at a distance of 54 nautical miles from the Indian landmass in Exclusive Economic Zane (EEZ) of India for carrying out fishing operations. (2 marks)

(b) State, with reason in brief, whether the following are liable to service tax :

(i) Penal interest charges

(ii) Services by an independent journalist

(iii) Technical testing of new drugs. (3 marks)

(iii) What are the demerits of VAT ? (5 marks)

Answer 4(a)

The Central Excise Tariff Act, 1985 is based upon HSN, but it is not a copy of HSN. In the case of *Camlin Ltd.* v/s *CCEX Mumbai* (2008) 230 ELT 193 (SC) the Apex Court ruled that when there is difference in the classification of any product between the entries of HSN and the Excisable Tariff, the classification as per the Central Excise Tariff Act, 1985 should be taken for the levy of excise duty. The department cannot rely upon HSN for classification. Therefore, the classification made by the department under HSN is not valid as per the law.

Answer 4(b)

The exemption notification is applicable only to imported goods. Imported goods means any goods brought into India through proper channel and licence. Goods imported without a licence are goods imported contrary to prohibitions under customs law. Such goods are liable to confiscation under section 111(d) of the Customs Act. Moreover, Customs Act defines imported goods and smuggled goods separately. Hence, there are two classes of goods. The smuggled goods are not imported goods. Therefore, the exemption notification is not applicable to the assessee who imported the goods without license. This was pronounced by the Apex Court in the case of *CC* v/s *M. Ambalal & Co.* (2010) 206 ELT 487 (SC).

Answer 4(c)

In this case the assessee i.e. Raj Sugar Ltd. is storing its own manufactured sugars in its godown as per the directions of the government. Basically, the company is a manufacturer of goods and not storage & warehouse keeper. The subsidy received from the government is not an income. It is an amount given to meet out certain expenses incurred by the assessee to maintain buffer stock as per the government directions. Further, the assessee has received subsidy not on account of services rendered to the government, but is paid as compensation on account of loss of interest, cost of maintenance, cost of insurance etc. Therefore, the subsidy is not taxable as it was also decided in the case of *CCE* v/s *Nahar Industrial Enterprises.* Therefore, the contention of the department is not valid as per law.

Answer 4A(i)

In order to claim the benefit of exemption under Notification No. 8/2003 – C.E. in a financial year, the total turnover of a unit should not exceed Rs. 400 lakh in the preceding financial year. As per Notification No. 8/2003 CE dated 1.03.2003, for the purpose of computing the turnover of Rs. 400 lakh;

(i) Turnover of non-excisable goods has to be excluded. Therefore, clearance of non-excisable goods of worth Rs. 100 lakh shall be excluded and not to be considered while computing the threshold limit of Rs. 400 lakh for claming SSI exemption.

(ii) Clearances made which are exempt under job work notification are not to be considered while computing the threshold limit of Rs. 400 lakh for claming SSI exemption. Therefore, exempt clearance of Rs. 75 lakh under job work notification will be excluded.

(iii) Export turnover is to be excluded AND export to Nepal AND USA is also to be treated as export turnover. (VIDE NOTIFICATION No. 8/2016 Dt. 1-3-2016)

(iv) Clearance of excisable goods of Rs. 275 lakh in the normal course will be considered while computing the threshold limit of Rs. 400 lakh for claming SSI exemption.

The turnover of Nargis Agro Ltd, for claiming the SSI exemption during the FY 2015-16 will be : Rs. 525 lakh – (Rs. 100 lakh + Rs. 75 Lakh + Rs. 75 Lakh) = 275 lakh.

Since, the turnover of Nargis Agro Ltd. in the preceding financial year 2014-15 is less than Rs. 400 lakh, it will be eligible for exemption under notification no. 8/2003 – CE in the current financial year.

Alternate Answer 4A(i)

In order to claim the benefit of exemption under Notification No. 8/2003 – C.E. in a financial year, the total turnover of a unit should not exceed Rs. 400 lakh in the preceding financial year. As per Notification No. 8/2003 CE dated 1.03.2003, for the purpose of computing the turnover of Rs. 400 lakh;

(i) Turnover of non-excisable goods has to be excluded. Therefore, clearance of non-excisable goods of worth Rs. 100 lakh shall be excluded and not to be considered while computing the threshold limit of Rs. 400 lakh for claming SSI exemption.

(ii) Clearances made which are exempt under job work notification are not to be considered while computing the threshold limit of Rs. 400 lakh for claming SSI exemption. Therefore, exempt clearance of Rs. 75 lakh under job work notification will be excluded.

(iii) Export turnover is to be excluded AND export to USA is also to be treated as export turnover.

(iv) Clearance of excisable goods of Rs. 275 lakh in the normal course will be considered while computing the threshold limit of Rs. 400 lakh for claming SSI exemption.

The turnover of Nargis Agro Ltd, for claiming the SSI exemption during the FY 2015-16 will be : Rs. 525 lakh – (Rs. 100 lakh + Rs. 75 Lakh + Rs. 50 Lakh) = 300 lakh.

Since, the turnover of Nargis Agro Ltd. in the preceding financial year 2014-15 is less than Rs. 400 lakh, it will be eligible for exemption under notification no. 8/2003 – CE in the current financial year.

Answer 4A(ii)

(a) Levy of service tax extends to whole of India except the state of Jammu and Kashmir and India means, inter alia, the vessels located in the continental shelf of India and the Exclusive Economic Zone of India, for the purposes of prospecting or extraction or production of mineral oil and natural gas and supply thereof.

Therefore, though the vessel is stationed at a distance of 54 nautical miles from Indian land mass in Exclusive Economic Zone (EEZ) of India, services provided there will not be liable to service tax as the vessel is used for carrying out fishing operations and not for oil/ natural gas.

(b) (i) Penal interest charges can get covered by tolerating an act which is declared service and hence taxable.

(ii) Services provided by an independent journalist are exempted from service tax as per Entry No. 17 of Notification No. 25/2012 dated 20.06.2012

(iii) Technical testing of new drugs is taxable from 11.07.2014. Earlier it was exempt under Entry No.7

Answer 4A(iii)

VAT has some demerits, such as follows:

- VAT is a multipoint tax. Credit may not be eligible if there is no proper evidence.
- VAT increases the cost of administration.
- Price may not be neutralized if the dealer does not follow the principles of VAT.
- Input Tax Credit not allowed for interstate purchases which results in cascading effect.
- It decreases the revenue of the department if proper checking of records of dealer is missing.

Question 5

(a) Who can make an application for settlement under the Central Excise Act, 1944? Can such an application be withdrawn ? (3 marks)

(b) State the relevant dates for determination of the rate of duty and tariff value for imports. (3 marks)

(c) Lion Traders, a registered dealer having stock of goods worth ₹60,000 purchased from outside the State, wishes to opt for Composition Scheme under the State VAT Act. Advise whether it is possible. (3 marks)

(d) *Vakil & Vakil, a firm of lawyers and solicitors rendered legal advice to Bipin, an architect and NPA Ltd., an advertising agency, during the month of October, 2015. Both Bipin and NPA Ltd. are not entitled for small service provider's exemption under the service tax in the financial year.*

Who is liable to pay service tax in this case ? Will your answer be different, if Bipin and NPA Ltd. sought legal advice from a lawyer, Ashish ? *(3 marks)*

(e) *Explain briefly how the terms 'warehouse', 'warehoused goods' and 'warehousing station' are defined in the Customs Act, 1962.* *(3 marks)*

Answer 5(a)

According to section 32E of Central Excise Act, 1944 an assessee in respect to a case relating to him may make an application to Settlement Commission under Central Excise Act, 1944 in such form and manner as prescribed. An assessee is defined under section 31(a) as any person who is liable to pay excise duty assessed under the Central Excise Act, 1944 and includes any manufacturer or producer of excisable goods or a registered person under the rules made or a private warehouse in which excisable goods are stored. Further, Section 32E(4) provides that an application once made for settlement cannot be withdrawn.

Answer 5(b)

Relevant date for determination of rate of duty and tariff value (Section 15):

- In case of goods entered for home consumption under section 46 – the date on which bill of entry is presented or the date of entry inwards whichever is later.
- In case of goods cleared from warehouse under section 68 – the date on which a bill of entry for home consumption is presented.
- In case of any other goods – the date of payment of duty.

Answer 5(c)

If a dealer wishes to opt for Composition Scheme, he should not have any stock of goods which are brought from outside the state on the day he exercises the option to pay tax by way under composition scheme. Hence, Lion Traders is not eligible to opt for composition scheme as it has goods worth Rs. 60,000 purchased from outside the state on the day it wishes to opt for the Composition Scheme.

Answer 5(d)

In case of taxable services provided or agreed to be provided to any business entity located in the taxable territory by an individual advocate or a firm of advocates by way of legal services, person liable to pay service tax is the person receiving such services i.e. would be taxable under Reverse Charge Mechanism.

Therefore, service tax will be payable by service receivers, Mr. Banerjee and NPA Ltd, irrespective of whether the legal advice is sought from Vakil and Vakil, a firm of lawyers or from Mr. Ashish an individual lawyer, irrespective of their turnover.

Note : Services provided by an individual advocate or a partnership firm of advocates by way of legal services to inter alia a business entity with a turnover up to Rs. 10 lakh in the preceding financial year are exempt from service tax.

In the given case, turnover of services of both Mr. Bipin and NPA Ltd. is more than Rs. 10 lakhs in the preceding financial year as they are not entitled to small service providers exemption in the said financial year and hence, legal services provided by Vakil and Vakil (firm of advocates) or Mr. Ashish (individual lawyer) during October, 2015 will not be exempt from service tax.

Answer 5(e)

As per section 2(43) of the Customs Act, 1962 'warehoused' means a public warehouse licensed under Section 57 or a private warehouse licensed under Section 58 or a special warehouse licensed under section 58A.

Section 2(44) of the Customs Act, 1962 defines "warehoused goods" to means goods deposited in a warehouse.

As per section 2(45) of the Customs Act, 1962 "warehousing station" means a place declared as a warehousing station under Section 9 of the Act.

Question 6

(a) Which was the first country to introduce Goods and Services Tax (GST) and When ? What are the functions of the GST Council in India ? (6 marks)

(b) Give reason in brief, in the context of provisions of VAT, whether following purchases are eligible for availing input tax credit :

(i) Rohit purchased goods from a registered dealer. He claims to have paid VAT, on the said goods but the invoice pertaining to said purchase has been lost because of negligence in his office.

(ii) Ankit purchased some capital goods. The final product manufactured by Ankit using these capital goods is exported out of India.

(iii) Mohit purchased goods from Sohan which are to be used in execution of a works contract.

(iv) Smile & Co. purchased goods from Manav Enterprises, a registered dealer. Manav Enterprises has opted for composition scheme under the provisions of respective State VAT Act.

(v) Sahil purchased goods from Ganesh. Ganesh has not shown VAT charged on the purchase value separately in the invoice. (1 mark each)

(c) State the allowability or otherwise of the following with respect to the provisions of the Customs Act, 1962 :

(i) Goods up ₹10,000 per passenger per visit can be purchased against rupee payment in duty free shop at an International Airport.

(ii) Bona fide baggage is exempt from duty.

(iii) Total customs duty on baggage is 30%.

(iv) Gifts through courier from abroad, not being prohibited goods, up to ₹5,000 can be imported duty free. (1 mark each)

Answer 6(a)

France was the pioneer who first introduced GST in the Year 1954.

Functions of the GST Council

- To recommend rate of taxes, cesses and surcharges to be levied by the Centre, States and local bodies.
- To list goods and services which may be subjected to or exempted from GST.
- To design model of GST laws and principles.
- To fix the threshold limit of turnover below which exemption may be given.
- To recommend the floor rates and special rates.
- To suggest special provisions for North East States and other hilly areas.

Answer 6(b)

(i) Input tax credit cannot be claimed on purchase made by Rohit as the purchase invoice is not available with him.

(ii) Capital goods used for manufacture / packing goods to be sold in the course of export out of the territory of India are eligible for claiming input tax credit. Thus, Ankit can claim input tax credit on capital goods purchased by him.

(iii) Mohit can claim input tax credit as purchase of goods for being used in execution of a works contract are eligible for input tax credit.

(iv) Purchases made by Smile & Co. from Manav Enterprises are not eligible for input tax credit as purchases from registered dealer who opts for composition scheme under the provisions of respective state VAT Act are not eligible for Input Tax Credit.

(v) Purchases made by Sahil are not eligible for input tax credit as the invoice issued by Ganesh does not show VAT charged on the purchase value separately in the Invoice.

Answer 6(c)(i)

False : Goods upto Rs. 5,000 per passenger per visit can be purchased against rupee in duty free shop at International Airport.

Answer 6(c)(ii)

True : Bona fide Baggage accompanying passenger is exempt from duty.

Answer 6(c)(iii)

False : Total Customs Duty on Baggage is Rs. 36.05%

Answer 6(c)(iv)

False : Gifts through courier or post can be imported duty free upto Rs. 10,000.

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DRAFTING, APPEARANCES AND PLEADINGS

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *Answer ALL Questions.*

Question 1

Comment on the following statements :

(a) A click-wrap agreement lacking bargaining power is not an enforceable contract in traditional sense.

(b) Certain basic principles are required to be followed in the construction of a will.

(c) Registration and payment of stamp duty on a deed of hire-purchase is compulsory.

(d) A debtor cannot claim or take advantage of non-payment of consideration for assignment. *(5 marks each)*

Answer 1(a)

The click-wrap or web-wrap agreements are those agreements which we generally come across while surfing internet such as "I AGREE" to the terms or "I DISAGREE" to the above conditions. A click-wrap agreement is mostly found as part of the installation process of software packages. It is also called a "click through" agreement or click-wrap license.

Icon Clicking where the user must click on an "OK" or "I agree" button on a dialog box or pop-up window. A user indicates rejection by clicking "Cancel" or closing the window. Upon rejection, the user can no longer use or purchase the product or service. A click wrap contract is a "take-it-or-leave-it" type of contract that lacks bargaining power. There is no scope for negotiation either to be accepted entirely or rejected entirely.

Click-wrap agreements are valid and enforceable contracts as far as offer and acceptance is concerned. Click-wrap agreements are contracts formed entirely over the Internet. Contracts are governed by the Indian Contract Act, 1872, but the e-contracts are governed under the Information Technology Act, 2000.

Answer 1(b)

There are two cardinal principles in the construction of Wills, deeds and other documents. The first is that clear and unambiguous dispositive words are not to be controlled or qualified by any general expression or intention. The second is, to use Lord Denham's language, that technical word or words of known legal import must have their legal effect even though the testator uses inconsistent words, unless those inconsistent words are of such a nature as to make it perfectly clear that the testator did not mean to use the technical terms in their proper sense.[*Lalit Mohan Singh Roy* v. *Chikkun Lai Roy*, ILR 24 Cal 834].

(i) *Cardinal maxim* : The cardinal maxim to be observed in construing a Will is to endeavour to ascertain the intentions of the testator. This intention has to be

primarily gathered from the document which is to be read as a whole without indulging in any conjecture or speculation as to what the testator would have done, if he had been better informed or better advised. [*Gnambal Ammal* v. *T. Raju Iyer*, AIR 1951 SC 103, 105].

(ii) Relevant considerations: In construing the language of a Will, the courts are entitled and bound to bear in mind other matters than merely the words used. They must consider the surrounding circumstances, the position of the testator, his family relationship, the probability that he would use words in a particular sense and many other things which are often summed up in somewhat picturesque figure. The court is entitled to put itself into the testator's arm chair. [*Venkatanarasimha* v. *Parthasarthy*, 41 IA 51, 70 (PC); *Gnambal Amma*l v. *T. Raju Iyer*, AIR 1951 SC 103,106].

(iii) Avoidance of intestacy: If two constructions are reasonably possible and one of them avoids intestacy while the other involves it, the court would certainly be justified in preferring that construction which avoids intestacy. [*Kasturi* v. Ponnammal, AIR 1961 SC 1302]. It is settled law that words in a Will must be construed in their ordinary grammatical sense unless it is shown that a clear intention to use them in a different sense exists and is so proved. [*Guruswami Pillai* v. Sivakami Ammal, AIR 1962 Mad 236].

(iv) Effect should be given to every disposition: It is one of the cardinal principles of construction of Will that to the extent that it is legally possible, effect should be given to every disposition contained in the Will unless the law prevents effect being given to it. The intention of the testator should be gathered by giving a harmonious interpretation to the various terms of the Will as a whole. [*Rampali* v. *Chando*, AIR 1966 All 584,586].

(v) Later part or last words to prevail in case parts irreconcilable or there is repugnancy. – If the several parts of the Will are absolutely irreconcilable, the part that is later has to prevail. [Section 88, Indian Succession Act, 1925; *Somasundera Mudaliar* v. *Ganga Bissen Soni*, 28 Mad 386]. In case of repugnancy, the last word in the Will shall prevail. [*CIT* v. *Indian Sugar Mills Association*, (1974) 97 ITR 486 SC)].

Answer 1(c)

There is no Article governing hire purchase agreement in Schedule I to the Indian Stamp Act. Such an agreement would, therefore, fall under the general Article 5 regarding agreements in general. A deed of hire-purchase is liable to stamp duty as an agreement under Article 5 of the Indian Stamp Act, 1899.

A hire purchase agreement or a hire agreement does not require registration under the Registration Act, 1908 as it relates to movable property.

Answer 1(d)

A debtor cannot claim or take advantage of non-payment of consideration for assignment. Section 130 of the Transfer of Property Act, 1882 specifically lays down that an assignment of an actionable claim may be with or without consideration. Passing of the property in the assigned property does not depend on the payment of consideration.

The question of payment of consideration is in fact one between the assignor and the assignee.

Section 132 of Transfer of Property Act provides that the transferee of an actionable claim shall take it subject to all the liabilities and equities to which the transfer was subject in respect thereof at the date of transfer.

Attempt all parts of either Q.No. 2 or Q.No. 2A

Question 2

Distinguish between the following :

(a) 'Public trust' and 'private trust'.

(b) 'Continuing guarantee' and 'counter guarantee'

(c) 'Probate' and 'letter of administration'.

(d) 'Operative clause' and 'testimonium clause'. *(4 marks each)*

OR (Alternate question to Q.No. 2)

Question 2A

Write notes on the following :

(i) Argument on merits

(ii) Need for a legal opinion

(iii) Appellate authorities under the Income-tax Act, 1961

(iv) Affidavit in evidence. *(4 marks each)*

Answer 2(a)

'Public trust' and 'private trust'

In a public trust the beneficiary is the general public or a specified section of it. In a private trust the beneficiaries are defined and ascertained individuals. In a public trust the beneficial interest is vested in an uncertain and fluctuating body of persons. The nature of the trust may be proved by the evidence of dedication or by user and conduct of parties. Where a trust is created for the benefit of the members of the settlor's family, it is a private trust and not a public trust. Every charitable trust is only a public trust as benefit to the community at large or to a section of the community is of the essence of a valid charitable trust. But a religious trust need not necessarily be a public trust as there can be a private religious trust also.

Answer 2(b)

'Continuing Guarantee' and 'counter guarantee'

Section 129 of the Indian Contract Act, 1872 lays down that a guarantee which extends to a series of transactions is called a continuing guarantee, and according to Section 130, a continuing guarantee may be revoked by the surety at any time as to future transactions, by notice to the creditor. A continuing guaranty may be revoked at any time by the guarantor in respect to future transactions, unless there is a continuing consideration as to the transactions that the guarantor does not give up.

A guarantee given by the principal debtor to the surety providing him indemnity against any damage that the surety may suffer on account of default on the part of the principal debtor is called 'counter guarantee'. Counter Guarantee is given by Banks normally on behalf of their customers to a third party. There are two types of Guarantee- Performance Guarantee and Financial Guarantee.

Answer 2(c)

'Probate' and 'letter of administration'

Probate is a certificate granted under the seal of Competent Court, certifying the Will as the Will of the testator and granting the administration of the estate of the deceased in accordance with that Will to the executor named under the Will. A will has no legal effect until it is probated. A will should be probated immediately, and no one has the right to suppress it.

A letter of administration can be obtained from the Court of competent jurisdiction in cases where the testator has failed to appoint an executor under a will or where the executor appointed under a will refuses to act or where he has died before or after proving the Will but before administration of the estate. Letters of Administration are not always necessary in cases of intestacy of Hindus, Mohammedans, Buddhists, Sikhs, Jains, Indian Christians or Parsis. Letter of Administration is always necessary where a person (governed by the Indian Succession Act) dies intestate.

Answer 2(d)

'Operative clause' and 'testimonium clause'

Operative clause is followed by the real operative words which vary according to the nature of the property and transaction involved therein. The words used in operative parts will differ from transaction to transaction. For example, in the case of mortgage the usual words to be used are "Transfer by way of simple mortgage" (usual mortgage) etc. The exact interest transferred is indicative after parcels by expressing the intent or by adding habendum. (The parcel is technical description of property transferred and it follows the operative words).

Testimonium is the clause in the last part of the deed. Testimonium signifies that the parties to the document have signed the deed. This clause marks the close of the deed and is an essential part of the deed.

The usual form of testimonium clause is as under:

"In witness whereof, parties hereto have hereunto set their respective hands and seals the date and year first above written". This is the usual English form of testimonium clause. In India, except in the case of companies and corporations seals are not used and in those cases testimonium clause reads as under:

"In witness whereof the parties hereto have signed this day on the date above written".

Thus testimonium clause can be worded according to the status and delegation of executants.

Answer 2A(i)

Arguments on Merits

The word merits refers to the substance of a legal dispute and not the technicalities that can affect a law suit. A judgment on the merits is the final resolution of a particular dispute. Then the judgment is rendered based upon the essential facts of the case, rather than on any technical or procedural rule, such as the failure of proper service. Such arguments as relate to the facts pleaded by the parties are termed as arguments on merits. While addressing arguments on merits, a lawyer/authorized representative should carefully point out the pleadings of the parties and the relevant evidence in support thereof, lead by the parties, both oral as well as documentary. A lawyer/ authorized representative should ensure that all or any contradiction in the pleadings of the opponent and the evidence in support of such pleadings are duly pointed out while submitting his/ her arguments. Thus, where an agreement/contract of service is pleaded and there is no evidence either oral or documentary on record in support of such an agreement/contract, it should be specifically pointed out that the opponent has failed to prove/establish that such an agreement/contract actually exists or that the same had actually been executed at all.

Similarly, where notice is alleged to have been served prior to filing of the case and there is no documentary evidence like postal receipt/courier receipt placed on record by the opponent, it should be pointed out that the opponent has failed to establish that the notice had actually been served. Furthermore, the relevant facts and/or contradictions extracted from the opponent or his/her witness during the course of cross-examination and relating to the factual issues involved in the matter, should be highlighted so as to draw attention of the Court/Tribunal towards such facts/contradictions.

Answer 2A(ii)

Need for a Legal Opinion

The need for a legal opinion arises from the following:

- Interpretation of statutes or documents
- Advise a transaction structure
- Opinion for guidance of decision makers in commerce, industry or government
- Opinion to Lenders on enforceability of Finance Documents
- Opinion for Investors for compliance by Target Companies
- Opinion on Foreign Direct Investment
- Determining provision for contingent liabilities or determination of contingent assets
- Merits or demerits of legal proceedings
- Provision for contingent liabilities or Identification of contingent assets
- Initiating civil or criminal proceedings
- Drafting a pleading

- Preparation for trial of arbitral or legal proceeding
- Ascertain compliance level for issue of securities and identification of risk factors for investors
- Valuation of business

Answer 2A(iii)

Appellate Authorities under the Income-Tax Act, 1961

Appeal against the order of the Income-tax Officer lies with the Appellate Assistant Commissioner or the Commissioner (Appeals) or Commissioner of Income-tax. Appeal against the order of the Appellate Assistant Commissioner or the Commissioner (Appeals) can be preferred by the assessee or the income-tax department and such appeal lies with the Appellate Tribunal. Appeal against the order of the Appellate Tribunal by way of reference by the Tribunal can also be preferred by the assessee or the income-tax department and such appeal lies to the High Court. The Order of the High Court on the reference can be challenged either by the assessee or by the income-tax department by preferring an appeal to the Supreme Court which is the final appellate authority.

Answer 2A(iv)

Affidavit in evidence

An affidavit is a type of verified statement. It contains a verification, meaning it is under oath or penalty of perjury, and this serves as evidence to its veracity and is required for court proceedings. It is well settled that evidence should be tailored strictly according to the pleadings. No extraneous evidence can be looked into in absence of specific pleadings. (*Habib Khan* v. *Valasula Devi*, AIR 1997 A.P 52).

The following must be kept in mind while preparing the affidavit-in-evidence by the parties –

(i) The best evidence is that of a person who was personally involved in the whole transaction. In case, that person is not available for any reason, then any other person who has joined in his place to make deposition by way of his affidavit.

(ii) In case, the petitioner himself was involved in the execution of a contract, he should file affidavit-in evidence.

(iii) The allegations or charges or grounds relating to facts should be re-produced duly supported by documentary evidence.

It may be noted that in the affidavit in evidence, the position of law or legal provisions or principle of law are not reproduced because the position of law or settled principles of law are not required to be proved by any party and they are deemed to exist and any party can argue and take help of those settled position of law while arguing their case before the Court or Tribunal or Forum and need to be proved by filing an evidence. [Section 5, Indian Evidence Act.]

(iv) In case, the point or issue pertains to engineering, medical, technology, science or other complex or difficult issues, then the evidence of expert is to be filed in the form of his Affidavit. If necessary, the said witness has to appear before the Forum for the purpose of cross-examination by the counsel for the other party. For example, hand-writing or finger print experts etc.

(v) Besides the leading evidence on the points raised by the petitioner or by the opposite party in his written statement/reply, if possible, the party who is filing the affidavit-in-evidence should also file documents, papers or books or registers to demolish the defence or case set up by the opposite party.

(vi) It is also permissible for any party to bring any outside witness (other than the expert witness) in support of his case if the facts and circumstances of the case so warrant and permitted by the Court/Tribunal.

(vii) At the time of tendering affidavit-in-evidence, the party must bring alongwith it either the original of papers, documents, books, registers relied upon by it or bring with it the carbon copy of the same.

It may be noted that only photocopy of any paper or document (in the absence of its reply, original or carbon copy) can not be relied upon and tendered as an evidence.

Attempt all ports of either Q.No. 3 or Q.No. 3A

Question 3

In the light of judicial pronouncements, discuss the following :

(a) Genuineness of information of an offence as a condition precedent for registration of offence under the Code of Criminal Procedure, 1973.

(b) A party can produce expert evidence in the cases involving complex or technical issues.

(c) Courts generally do not grant relief, if not prayed for.

(d) A will and codicil are one and the same. (4 marks each)

OR (Alternate question to Q.No. 3)

Question 3A

Comment on the following with reference to ratio in leading cases, if any :

(i) A sub-lease is an absolute assignment under the Indian law or the English law.

(ii) An HUF can become a partner in a firm.

(iii) Shareholders' agreements are generally not enforceable in India.

(iv) Pre-requisites of arbitration. (4 marks each)

Answer 3(a)

Registration of FIR is mandated in Section 154 of the Criminal Procedure Code, 1973, which clearly lays down that:

Every information relating to the commission of a cognizable offence, if given orally to an officer in charge of a police station, shall be reduced to writing by him or under his direction, and be read over to the informant; and every such information, whether given in writing or reduced to writing as aforesaid, shall be signed by the person giving it, and the substance thereof shall be entered in a book to be kept by such officer in such form as the State Government may prescribe in this behalf.

The provision of Section 154 of Code of Criminal Procedure, 1973 is mandatory.

Hence, the police officer concerned is duty-bound to register the case on receiving information disclosing cognizable offence. Genuineness or credibility of the information is not a condition precedent for registration of a case. That can only be considered after registration of the case. [*Ramesh Kumari* v. *State (NCT of Delhi) and Ors.*, 2006 Cri.LJ 1622].

Answer 3(b)

It is incumbent upon a party to produce evidence of some expert where the issue involved is a complex or difficult one as for instance, issues pertaining to engineering, medical, technology or science etc. Since the court can not constitute itself into an expert body and contradict the claim/proposition on record unless there is something contrary on the record by way of expert opinion or there is any significantly acclaimed publication or treatise on which reliance could be based. [*Dr. Harkanwaljit Singh Saini* v. *Gurbax Singh & Anr.*, 2003 NCJ 800 (NC)]

Answer 3(c)

A plain reading of Order VII Rule 7 makes it clear that it is primarily concerned with drafting of relief in a plaint. It is in three parts -- the first part directs that the relief claimed by the plaintiff simply or in the alternative shall be stated specifically. It incorporates in the second part the well settled principle that it shall not be necessary to ask for general or other relief which may always be given as the Court may think just on the facts of the case to the same extent as if it has been asked for. The third part says that in regard to any relief claimed by the defendant in his written statement, the same rule shall apply.

Rule 7 of Order VII - Code of Civil Procedure, 1908 says that every plaint shall state specifically the relief which the plaintiff claims either simply or in the alternative, and it shall not be necessary to ask for general or other relief which may always be given as the Court may think just to the same extent as if it had been asked for. And the same rule shall apply to any relief claimed by the defendant in his written statement. {*Rajendra Tiwary*, vs. *Basudeo Prasad and Another*, AIR 2002 SC 136}

The Supreme Court in *Shehla Burney* vs. *Syed Ali Mossa Raza* has reiterated that no relief can be granted against a party unless it has been specifically claimed in the suit or petition, as mandated by Order VII Rule(s) 5 & 7 of the Code of Civil Procedure.

Rule 8 of Order VII - Code of Civil Procedure, 1908 says that if the plaintiff seeks relief in respect of several distinct claims or causes of action founded upon separate and district grounds, they shall be stated as far as may be separately and distinctly.

Answer 3(d)

A will and codicil are not one and the same. 'Will' means the legal declaration of the intention of a testator with respect to his property, which he desires to be carried into effect after his death [Section 2(h) of Indian Succession Act, 1925]. A Will is, therefore, the legal declaration of a man's intention which he wills to be performed after his death or an instrument by which a person makes a disposition of his property to take effect after his death. 'Will' as per General Clause Act, 1897 shall include a Codicil and every writing making a voluntary posthumous disposition of property.

Codicil is a supplement or addition to a will that explains, modifies, or revokes a

previous will provision or that adds an additional provision. A codicil must be signed and witnessed with the same formalities as those used in the will's preparation. An addition or supplement to a will; it must be executed with the same solemnities. A codicil is a part of the will, the two instruments making but one will. There may be several codicils to one will and the whole will be taken as one: the codicil does not consequently revoke the will further than it is in opposition to some of its particular dispositions, unless there are express words of revocation. 'Codicil' means an instrument made in relation to Will and explaining, altering or adding to its dispositions and is deemed to form part of the Will – Section 2(d) of Indian Succession Act, 1925.

Answer 3A(i)

An absolute assignment is the act of complete transfer of the ownership (all rights, benefits and liabilities) of the policy completely to other party without any terms and condition. Generally, Sub-lease of property is made by a person who is himself a lessee or tenant of that property. A sublease may be prohibited by the original lease, or require written permission from the owner.

A sub-lease is demise by a lessee for lessor term than he himself has. If the demise is for the whole term or for a period beyond the term, it amounts to assignment. The Privy Council pointed out in *Hunsrai* v. *Bejoylal Seal*, (1930) 57 Cal 1176, that in India a sub-lease is not an absolute assignment and it was further held in *Akshoy Kumar* v. *Akman Molla*, (1915) 19 CWN 1197, that there is no privity of estate as between the lessor and the sub-lessee, who does not step into the shoes of the lessee.

Answer 3A(ii)

The word "person" in Section 4 of the Indian Partnership Act, 1932 contemplated only natural and legal persons. (*Duli Chand* v. *C.I.T.*, AIR, 1956 SC 354). Partnership relation is one of contractual nature. Therefore, such persons who are competent to contract can enter into partnership.

Therefore, a HUF is not a person as defined in Section 4 of the Indian Partnership Act, 1932 and cannot enter into partnership with any person. However, Karta on behalf of HUF can become partner in the partnership firm. But, when the Karta of a HUF enters into partnership with strangers, the other members of the HUF do not ipso facto become partners. (*Firm Bhagat Ram* vs. *Comm. of Excess Profits Tax*, AIR 1956 SC 374)

Answer 3A(iii)

Shareholders' agreements (SHA) are quite common in business. In India shareholder's agreement have gained popularity and currency only lately with bloom in newer forms of businesses. Shareholders' agreement is a contractual arrangement between the shareholders of a company describing how the company should be operated and the defining inter-se shareholders' rights and obligations. A SHA creates personal obligation between the members signing such agreement however, such agreements do not become a regulation of the company in the way the provisions of Articles are.

Though the international views on enforceability of SHA are split but to a large extent courts are inclined towards favouring SHA as long as they are not found to be detrimental to the minority stakeholder's rights. The US Courts have largely accepted shareholder agreements. [*Blount* v. *Taft* [246 S.E.2d 763 at 769 (1978)]

While shareholders' agreements are enforceable in England regardless of whether they have been incorporated in the articles of association of the company, in India courts have either refused to recognize clauses in shareholders agreements or, even when consistent with company legislation, enforced such clauses only if they have been incorporated in the articles of association of the company. There is a series of rulings where the courts have upheld that in case of any conflict between the Articles and the SHA, the former will always prevail.

The Supreme Court in *V.B. Rangaraj* v. *V.B. Gopalakrishnan*, AIR 1992 SC 453 held that a restriction which is not specified in the articles of association is not binding either on the company or on the shareholders. This decision was reiterated by the Bombay High Court in *IL & FS Trust Co. Ltd.* v. *Birla Perucchini Ltd.* [2004] 121 Comp Cas 335 (Bom).

Answer 3A(iv)

Arbitration has been defined as a mode of settlement by referring a dispute to a tribunal of the parties' own choice without them having to resort to a court of law.

Every arbitration must have the following three pre-requisites:

(i) a dispute between parties to an agreement, requiring a settlement;

(ii) its submission for a settlement to a third person; and

(iii) a decision by such third person according to his own judgement based on the facts and circumstances of the dispute, which is binding on both the parties.

(iv) There should be a valid and binding agreement between the parties.

Question 4

(a) VT Ltd. instituted a suit against KA Furnitures Ltd. for breach of contract for supply of 200 study tables priced at ₹500 per table, on the following three counts:

(i) KA Furnitures Ltd. did not supply full order within the stipulated time of three months from the date of contract.

(ii) The wood used for making the tables was not as per agreed specifications, instead of sheesham wood, neem wood was used.

(iii) Legs of 50 tables were found bent and weak.

All this occasioned a heavy loss of ₹25,000, which was claimed with interest @10% per annum and costs in the suit against defendants.

The defendant, KA Furnitures Ltd., refuted the claim made in the plaint by stating in written statement that "the defendant generally denies the allegations made by plaintiff as got up and unsustainable". Explain with reasons whether this defense would sustain in courts. (8 marks)

(b) Anil took a loan of 10 lakh from JF Financial Corporation (a registered financial company) for purchasing a one bed room flat on an agreed rate of interest of 16% per annum. Along with agreement papers, a promissory note (P/N) was signed by Anil which read, "Anil has taken loan of ₹10 lakh from JF Financial

Corporation for purchasing a flat and whenever JF Financial Corporation demands its return, Anil shall pay back in ten instalments to them or to barer of this PA.

After one year, Anil defaulted in return of loan on demand by JF Financial Corporation. Consequently, a summary suit was instituted by JF Financial Corporation against Anil in the Court of Civil Judge. After scrutiny, the court dismissed the suit holding that the P/N was void.

What drafting precautions ought to have been taken by JF Financial Corporation when Anil was executing the P/N payable on demand ? Cite the relevant case law if any. *(8 marks)*

Answer 4(a)

It is necessary that one has to deny the averment of the plaint/petition which are incorrect or false. In case any averment contained in any paragraph of the plaint is not denied specifically, it is then presumed to have been admitted by the other party. (Order 8, Rule 5 of Code of Civil Procedure).

It must be borne in mind that the denial has to be specific and not evasive or general. (Order 8, Rules 3 & 4 of CPC). This has been reiterated in *Dalvir Singh Dhilowa*l v. *Kanwaljit Singh* 2002 (1) Civil LJ 245 (P&H); *Badat & Co.* v. *East India Trading Co.* AIR 1964 SC 538. However, general allegation in the plaint cannot be said to be admitted because of general denial in written statement. [*Union* v. *A. Pandurang,* AIR 1962 SC 630.]

It shall not be sufficient for a defendant in his written statement to deny generally the grounds alleged by the plaintiff, but the defendant must deal specifically with each allegation of fact of which he does not admit the truth, except damages.

Thus, where a defendant denies an allegation of fact in the plaint, he must not do so evasively, but answer the point of substance.

In the light of the above, the general refutation and denial made by KA Furniture Ltd. against the specific averments of VT Ltd are not valid.

Answer 4(b)

Promissory note is one of the negotiable instruments recognized under the Negotiable Instruments Act, 1881. A "promissory note" is defined by Section 4 of the Negotiable Instruments Act, 1881 as "an instrument in writing (not being a bank note or a currency note) containing an unconditional undertaking, signed by the maker to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument".

To be a promissory note, an instrument must possess the following essentials:

(a) It must be in writing. An oral promise to pay will not do.

(b) It must contain an express promise or clear undertaking to pay. A promise to pay cannot be inferred. A mere acknowledgement of debt is not sufficient. If A writes to B

"I owe you (I.O.U.) Rs. 500", there is no promise to pay and the instrument is not a promissory note.

(c) The promise or undertaking to pay must be unconditional. For example : A promise to pay "when able", or "as soon as possible", or "after your marriage to D", is conditional. But a promise to pay after a specific time or on the happening of an event which must happen, is not conditional, e.g. "I promise to pay Rs. 1,000 ten days after the death of B", is unconditional.

(d) The maker must sign the promissory note in token of an undertaking to pay to the payee or his order.

(e) The maker must be a certain person, i.e., the note must show clearly who is the person engaging himself to pay.

(f) The payee must be certain. The promissory note must contain a promise to pay to some person or persons ascertained by name or designation or to their order.

(g) The sum payable must be certain and the amount must not be capable of contingent additions or subtractions. If A promises to pay Rs. 100 and all other sums which shall become due to him, the instrument is not a promissory note.

(h) Payment must be in legal money of the country. Thus, a promise to pay Rs. 500 and deliver 10 quintals of rice is not a promissory note.

(i) It must be properly stamped in accordance with the provisions of the Indian Stamp Act. Each stamp must be duly cancelled by maker's signature or initials.

(j) It must contain the name of place, number and the date on which it is made. However, their omission will not render the instrument invalid, e.g. if it is undated, it is deemed to be dated on the date of delivery.

A promissory note cannot be made payable or issued to bearer, no matter whether it is payable on demand or after a certain time (Section 31 of the RBI Act).

In the light of the above, JF Financial Corporation ought to have taken the above precautions at the time of execution of Promissory note (P/N).

Question 5

(a) In a pending suit for recovery of possession of house, the defendant filed written statement denying plaintiffs right of recovery. A list of four witnesses, two of whom were employees of Municipal Corporation was also filed. It was approved by the court. Summons to two defence witnesses (DWs) were issued by court. They were duly examined. But the court, in a cryptic unreasoned order, refused to summon remaining DWs with public record in defense of the defendant, and closed the evidence stage.

Draft a specimen revision petition to cure this defect in the trial of the suit and, thus, to prevent the miscarriage of justice. Assume hypothetical data,if necessary. (8 marks)

(b) What is the law relating to nomination of a successor to a partner of a firm in the event of death/retirement of the existing partner ? (4 marks)

(c) Explain, with example, the scope of interlocutory applications filed by the parties in courts. Cite applicable law, if any. (4 marks)

Answer 5(a)

SPECIMEN FORM OF REVISION

In the High Court of ……..

Civil Appellate Jurisdiction

Civil Revision No …….. of 2016

IN THE MATTER OF:

ABC S/o……..…… R/o……

Petitioner

Versus

XYZ S/o..... R/o……

…Respondent

AND

IN THE MATTER OF:

CIVIL REVISION AGAINST THE ORDER DATED…… PASSED BY THE LEARNED SUB-JUDGE, IST CLASS…….. IN THE SUIT ENTITLED ABC -VS.- XYZ (CIVIL SUIT NO. …… OF 2016)

May it please the Hon'ble Chief Justice, High Court of…… and his companion Justices.

The petitioner MOST RESPECTFULLY SHOWETH:

A. That the petitioner named above has filed a suit against the respondents for the recovery of possession of a house situated in……, fully described in the plaint. The suit is pending in the court of Sub-Judge Ist Class…… and the next date of hearing is……

B. That on being summoned the defended appeared before the court below and filed his written statement wherein he denied the petitioner's right of recovery. A list of four witnesses, two of whom were employees of Municipal Corporation was also filed.

C. That the trial court framed issues on…… and summoned two defence witnesses.

D. That on a previous date of hearing that is……, 2016, two defence witnesses duly examined. However, the learned Presiding Officer of the court below, in a cryptic unreasoned order, refused to summon remaining defence witnesses with public record in defence of the defendant.

E. That on the next date of hearing the learned trial court by the order impugned in this revision closed the evidence stage.

F. That the impugned order has caused great prejudice to the petitioner and if the same is allowed to stand the petitioner's suit is bound to fail.

In the facts and circumstances discussed above the petitioner prays that this Hon'ble Court be pleased to quash and set aside the order under revision and direct the court below to provide assistance of the court for summoning the plaintiff witnesses.

PETITIONER

[Affidavit to be filed in support of the fact that the contents of the accompanying revision petition are true and correct to the best of the deponent's knowledge and that nothing has been kept back or concealed].

Answer 5(b)

It is not uncommon in partnership agreements to find a clause as to nomination of a successor who has the right to be declared and admitted as partner in the event of death or retirement of a partner. It was, however, held by the Supreme Court in *Commissioner of Income Tax* v. *Govindram Sugar Mills*, AIR 1966 SC 24, that the nomination is not effective in case of partnership firm consisting of two partners only as it stands dissolved on the death of a partner; nevertheless, in view of the rights and obligations of a person to be nominated as under Section 31 of the Act, the same principle in case of agreement between two persons is applicable in case of partnership between two partners.

Answer 5(c)

"Interlocutory" means not that decides the cause but which only settles some intervening matter relating to the cause. After the suit is instituted by the plaintiff and before it is finally disposed off, the court may make interlocutory orders as may appear to the court to be just and convenient. The power to grant Interlocutory orders can be traced to Section 94 of C.P.C. Section 94 summarises general powers of a civil court in regard to different types of Interlocutory orders. The detailed procedure has been set out in the Schedule I of the C.P.C which deals with Orders and Rules. Interlocutory orders may take various shapes depending upon the requirement of the respective parties during the pendency of the suit. Applications for appointment of Commissioner, Temporary Injunctions, Receivers, payment into court, security for cause etc. are the examples of such application.

An interlocutory application is an application which is moved in the main petition. It is usually filed when you ask for some urgent relief or to bring certain new facts to the knowledge of the court. An Interlocutory Petition is initiated with a view to prevent the ends of justice from being defeated when the Original Petition is unable to address the immediate circumstances. Interlocutory Applications or Interlocutory Petitions are filed to support the main petition for an interlocutory relief during pendency of the main Petition.

Question 6

(a) In a seminar on 'appearance in courts', the keynote speaker highlighted the significance of dress code for a Company Secretary appearing in courts representing his company-in-lis. A debate set in when a lady CS insisted that there should be no dress code for ladies while appearing before Courts/Tribunals.

Explain the importance of professional dress code and state the guidelines for professional dress of Company Secretaries. (8 marks)

(b) Dilip, the owner of a bungalow in Salt Lake area of Kolkata, decided to let-out his bungalow with 1,000 sq. feet area abutting 60 feet wide main road to QRS Corporation, for a term of three years on a rent of ₹1,00,000 per month plus taxes, service charges, etc. thereon. The premises is to be used for office accommodation purposes only. Protecting the interests of all concerned parties, draft a specimen 'agreement of licence' to use the property. Assume supplementary data as may be required. (8 marks)

Answer 6(a)

Importance of Professional Dress Code

In professional life it is important to look presentable because personal appearance counts. How you look can be a major factor in how you are perceived by others. How you look, talk, act and work determines whether you are a professional or an amateur. The way you dress, speaks volumes about who you are as a person and as a professional. Whenever you enter a room for the first time, it takes only a few seconds for people you have never met to form perceptions about you and your abilities. Your clothes and body language always speak first. So it is important that your image gives people the right impression.

A dress code is a set of rules governing a certain combination of clothing. Apart from the legal profession, professional dress code standards are established in major business organizations and these have become more relaxed in recent decades. Dress codes vary greatly from company to company, as different working environments demand different styles of attire. Even within companies, dress codes can vary among positions.

Getting dressed for work is to project a professional and competent image. It has been observed that the professionals who do not take the time to maintain a professional appearance or those who have never learned how to dress properly for their chosen field of work, are not being taken seriously by co-workers and present the image of not being able to perform satisfactorily on the job.

If you are concerned about your career, you will be more concerned with looking professional than looking cute or trendy. If you look and behave like a highly-trained and well-groomed professional, you will win the respect and honour of your valued clients.

Guidelines for Professional Dress of Company Secretaries

To enhance the visibility and brand building of the profession and ensuring uniformity, the Council of the Institute of Company Secretaries of India has prescribed the following guidelines for professional dress for members while appearing before judicial/quasi-judicial bodies and tribunals:

(a) The professional dress for male members will be Navy Blue suit and white shirt with a tie (preferably of the ICSI) or navy blue buttoned-up coat over a pant or a navy blue safari suit.

(b) The professional dress for female members will be saree or any other dress of a sober colour with a navy blue jacket.

(c) Members in employment may wear the dress/uniform as specified by the employer for all employees or if allowed the aforesaid professional dress.

(d) Practising Company Secretaries appearing before any tribunal or quasi-judicial body should adhere to dress code if any prescribed for appearing before such tribunal or quasi-judicial body or if allowed the aforesaid professional dress.

Answer 6(b)

SPECIMEN AGREEMENT OF LICENSE FOR USE OF A HOUSE PROPERTY TO A COMPANY FOR OFFICE ACCOMMODATION

AN AGREEMENT MADE this…… day of…..…… 2016 BETWEEN Dilip son of……. R/o ……by faith…… by occupation……. herein after referred to as the "owner" of the ONE PART AND QRS Corporation represented by Mr. ..... its secretary being signatory to this agreement having its principal office at present at No..... hereinafter referred to as "occupiers" of the OTHER PART.

WHEREAS the occupiers approached the owner for permission for using of his property, viz. bunglow No. ..... in Salt Lake, Kolkata fully mentioned and described in the Schedule hereto for a period not exceeding three years only from the date of signing of this agreement which the owner has agreed to grant reserving for himself the care, maintenance and services to property and on the basis of leave and license only (which will stand ipso facto revoked on the expiry of the said term). Now, it is hereby expressly agreed and declared by and between the parties as follows:

1. This writing shall never be construed as any tenancy agreement or lease nor otherwise creating any other right or interest in the property in favour of the occupiers which is not at all the intention of the parties but on the contrary merely a temporary agreement or arrangement simply to allow the occupiers to use and occupy portion of the premises for their office accommodation under the control and supervision of the owner for which purpose the owner shall retain..... rooms, viz., one in the ground floor and another in the first floor. The owner shall have his own staff in the said rooms for the care and supervision and maintenance of and services to the property.

2. The occupiers shall, in consideration of such accommodation as hereunder provided, pay to the owner a fixed sum of Rs. 1,00,000/- per month plus taxes, service charges etc. as charges for such temporary occupation for the period of three years after deducting TDS as applicable.

3. The occupiers shall also pay to the owner on account of Corporation of Kolkata all existing and future occupiers' share of rate and taxes of the property and also the enhancement in the owner's share, if any, during the period of their occupation and shall otherwise keep the owner and his estate indemnified as against any loss, if any, arising out of such non-payment or non-observance of any of the covenants herein contained.

4. The occupiers have as security deposit for such payments and observance of the covenants hereunder contained, kept with the owner a sum of Rs..... to be repaid without interest on revocation of license and surrender and deliver the possession of the said portion of the property subject to such deductions as the owner shall be entitled as against the occupiers. e.g., arrears of charges

provided in Clause 2, unpaid taxes, electric bills, etc., as hereunder provided or otherwise permitted in law.

5. The occupiers shall on expiry of the period of……..... and license hereunder granted or earlier revocation thereof, surrender the property and deliver the same to the owner when and in such an event he will be entitled to the refund of Rs..... subject to deductions provided in Clause 4 hereof.
6. Provided, however, and notwithstanding anything hereinbefore contained, it is hereby expressly agreed by and between the parties hereto that in default of any payment on the dates hereinbefore referred to above to the owner or the Corporation of Kolkata or other appropriate authorities the owner shall be entitled to and shall have always the power to revoke the license hereunder granted at his absolute discretion and reoccupy the said portion of the property without subjecting himself to any liability on that account and notwithstanding any intermediate negotiations or waiver of breach thereof when and in such an event the occupiers shall surrender the occupied portion of the property as hereunder contemplated.
7. The occupiers shall have no right to make any addition or alteration to the property except temporary removable walls by way of adjustments but shall be entitled to make interior decorations only by temporary wooden partitions which they shall remove at their own costs at the time of surrender of the said portion of the property on expiry of the term of the license hereby granted or earlier revocation thereof and repairs all the damages, if any caused to the property.

IN WITNESS WHEREOF the parties have executed this Agreement on this ..... day of 2016

Signed, sealed and delivered at Kolkata

In the presence of

(1)

(2)

(3)

***

BANKING LAW AND PRACTICE

(Elective Paper 9.1)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Read the following comprehension and answer the questions that follow :

BANK GUARANTEE

The liability of the bank under a guarantee depends on two fundamental criteria, viz., the amount guaranteed and the period of guarantee. These two factors have to be specifically stated since in the absence of any one or both of these factors the bank's liability could be unlimited, either in the amount guaranteed or the period during the guarantee. The banker should also obtain counter guarantee from his customer on whose behalf he has given the guarantee, so that in case he is required to pay the guarantee he can fall back on the counter guarantee to claim the amount paid by him.

Amount guaranteed

When the bank issues a guarantee, the first and foremost consideration that should weigh in a banker's mind is the amount of guarantee he is called upon to issue. In the guarantee agreement, the amount has to be specifically stated, both in figures and words. While stating the amount that the bank would guarantee to pay, care should be taken to state whether the amount is inclusive of all interest, charges, taxes and other levies. This is important to avoid unnecessary disputes regarding liability of the bank. On invocation, the bank is liable to pay whole amount of the guarantee, unless an earlier case of fraud has been brought to its notice.

One more point deserves to be considered here with reference to guarantee i.e., right of general lien becoming that of particular lien. Banker's right of general lien is displaced by circumstances which show an implied agreement being inconsistent with the right of general lien. In Vijay Kumar v. M/s. Jullundur Body Builders, Delhi and Others [A.I.R. 1981, Delhi 126], the Syndicate Bank furnished a bank guarantee for ₹90,000 on behalf of its customer. The customer deposited with it as security, two fixed deposit receipts, duly discharged, with a covering letter stating that the said deposits would remain with the bank so long as any amount was due to the bank from the customer. Bank made an entry on the reverse of receipt as "Lien to BG 11/80'. When the bank guarantee was discharged, the bank claimed its right of general lien on the fixed deposit receipt, which was opposed on the ground that the entry on the reverse of the letter resulted in the right of a particular lien, i.e., only in respect of bank guarantee.

The Delhi High Court rejected the claim of the bank and held that the letter of the customer was on the usual printed form while the words written by the officer of the bank on the reverse of the deposit receipt were specific and explicit. They are the

controlling words, which unambiguously tell us what was in the minds of the parties at the time. Thus, the written word prevail over the printed 'word'. The right of the banker was deemed to be that of particular lien rather than of general lien.

Period of guarantee

Banks always specify the period for which their guarantee subsists and an additional period during which a claim has to be made on the bank to make payment. The former period during which the guarantee subsists is called the 'validity period' and the latter, the 'claim period'. If any default has been committed by the debtor (i.e., the bank's customer), it should be within the validity period. It is, thus, necessary as a matter of great caution that this period be specified to t}re exact date, for example, "this guarantee is valid up to 31st December, 2017".

Once this outer limit for the bank to guarantee a default of the debtor is fixed then the creditor can make a claim only if the default has occurred within this period; and for any default other than this period, bank cannot be held liable. Once a default is made then the surety has to make a claim on the bank to make good the loss within the claim period.

Claim period in a guarantee

In a guarantee, it is necessary to provide for a period slightly longer than the validity period for the beneficiary to make a claim. The claim period is usually a few months more than the validity period of the guarantee. Since if the debtor was to commit a default on the last day of the validity period, then the beneficiary can at the earliest invoke the same only on the next day. Taking into account the time to communicate the invocation, etc., the claim period should at least be 15 to 30 days more than the validity period. For example, if the validity period of the guarantee is up to 31st December, 2017, then the claim period would normally be up to 31st January, 2018.

Amendment to section 28 of the Indian Contract Act, IE72 and its effect on bank guarantee

Prior to the amendment of section 28 of the Indian Contract Act, 1872, most bank guarantees had a standard clause at the end of their guarantee agreements. As per this clause, the beneficiary was required to enforce his claims within a period of 3 to 6 months, failing which the bank's liability was extinguished and hence, the rights of the beneficiary. The above clause was necessitated due to the fact that in absence of it, government departments and municipal bodies need to file a suit against the bank under bank guarantee within a period of 30 years after making claim. The bank would, therefore, be required to carry forward this liability for a long period and thereby required to make provision for the same in the balance sheet. Added to this, the customer's cash margin and security would have to be retained either till the guarantee is returned by the beneficiary or till the expiration of the period of limitation.

Though this clause had been challenged before various High Courts, the High Courts have held such clauses in the bank guarantees to be valid and not violative of section 28 of the Indian Contract Act, 1872.

However, from 1st January, 1997, section 28 of the Indian Contract Act, 1872 has been amended due to which the standard limitation clauses in the bank guarantees through which the banks extinguished their liability has been declared illegal. As such, at present if a beneficiary was to invoke the guarantee within the claim period,

for a default committed by the debtor during the validity period then in case the bank did not make payment, the beneficiary can sue the bank within normal period as provided in the Limitation Act, 1963. This period under the Limitation Act, 1963 is 30 years in case the beneficiary is a government department or municipal body and 3 years in all other cases.

Therefore, it is prudent to insist that the bank guarantee be returned after the claim period, duly cancelled by the beneficiary or a certificate be obtained from the beneficiary that there are no claims under the guarantee; till such time the cash margin and the security of the debtor (customer) has to be retained.

Counter guarantee and other security

Though a bank guarantee is a contingent liability, it is always prudent for a banker to securethis contingent liability in case it is enforced. This can be done by obtaining a counter guarantee cum-indemnity executed by the customer in favour of the bank. The counter guarantee cum indemnity should be carefully drafted to ensure that in case the banks were to make payment on behalf of the customer then the customer in turn should not only make good the amount paid by the bank to the creditor but also any expenses connected therewith including cost of the attorney, any interest on the delayed payment, taxes and other levies. It is to take care of all the above payments that the counter guarantee also includes an indemnity aspect. The counter guarantee should also include a clause that it would remain in force till the guarantee given by the bank subsists, viz., till the bank is duly discharged by the beneficiary or a certificate to this effect is issued by the beneficiary.

Though the counter guarantee-cam-indemnity is taken as security for every guarantee issued by the bank, its value would depend on the financial standing of the person/ company giving the counter guarantee. Hence, it is preferable that keeping in mind the financial worth of the counter guarantor, necessary security in the form of fxed deposits, mortgage, etc. be obtained or the existing charge of the debtor be extended to cover the guarantee.

Payment under bank guarantee

Before making payment, a banker has to ensure that the invocation of the guarantee has been properly done failing which he may not have any recourse against the debtor. The banker should also see that no order of injunction has been passed by any r ourt of law prohibiting the bank from making payment. In case a banker makes payment in spite of there being an order by a competent court in which the bank is a party, then the bank will be answerable for contempt of court.

Questions -

(a) Banks issue different types of guarantees on behalf of their customers. Briefly explain the nature of each type of bank guarantee. (10 marks)

(b) State in brief the precautions to be taken by the banks - (i) while issuing a bank guarantee; and (ii) before making payment under the bank guarantee. (10 marks)

(c) What requirements a banker should ensure in deciding whether the invocation made is proper in case of payment under a bank guarantee ? (5 marks)

(d) While issuing a guarantee the bank omits to mention the amount and period of

the guarantee. Can the bank still be held liable ? What would be the extent of liability ? *(5 marks)*

(e) What is 'validity period' and 'claim period' in a bank guarantee ? *(5 marks)*

(f) Can the bank in a guarantee issued by it restrict the claim period so as to avoid its liability ? Discuss. *(5 marks)*

(g) What is a counter guarantee and when is it obtained ? *(5 marks)*

(h) What is an order of injunction ? *(5 marks)*

Answer 1

(a) Guarantees issued by banks are mainly Financial Guarantee, Performance Guarantee and Deferred Payment Guarantee.

Financial Guarantee

The banker issues guarantee in favour of a government department against caution deposit or earnest money to be deposited by bank's client. At the request of the customer, in lieu of a caution deposit or earnest money, the banker issues a guarantee in favour of the government department. This is an example of a Financial Guarantee. This type of guarantee helps the bank's customer to bid for the contract without depositing actual money. In case, the contractor does not take up the awarded contract, then the government department would invoke the guarantee and claim the money from the bank.

Performance Guarantee

Under performance guarantee, the bank as guarantor guarantees the beneficiary that in case the applicant does not perform to the satisfaction of the beneficiary, within the validity period (including the claim period if any) of the guarantee, the beneficiary can invoke the guarantee and the banker has to honor his commitment and pay the amount mentioned in the guarantee.

Deferred Payment Guarantee

Under this type of guarantee, the banker guarantees payment of installments spread over a period of time. This type of guarantee is required when goods or machinery is purchased by a customer on credit and the payment is to be made in installments on specified dates as per schedule drawn in the contract agreed upon.

For example : Mr. A purchases a machinery on a long-term credit basis and agrees to pay the cost in installments on specified dates as pre- scheduled over a period of time. In terms of the contract of sale, Mr. B (the seller) draws Bills of Exchange on the customer for different maturities. These bills are to be accepted by Mr. A. The banker (guarantor) guarantees payment of these bills of exchange on the due date. In the event of default by Mr. A, the banker need to honor the claim to the seller (beneficiary).Again this has a time limit for the claim.

(b) Precautions to be taken by banks –

(i) *While issuing a bank guarantee* - It has to be ensured that the amount guaranteed

and the period of the guarantee is specially mentioned in the guarantee. These two are important factors to be clearly mentioned in the guarantee issued by the banker, otherwise the bank's liability could be unlimited. The bank should obtain a counter guarantee from the customer on whose behalf guarantee is issued, because this helps in claiming the guarantee from the beneficiary who is originally liable for it. This is to doubly insure the fund parted with by the bank and it also provides a legal tool to claim it, if not paid. At the time of issuing the guarantee, the amount to be paid under the guarantee should clearly state whether the amount is inclusive of all interest charges, taxes and other levies to avoid disputes regarding the liability of the bank.

On invocation (claim made by the beneficiary), the bank is liable to pay the entire amount of the guarantee except in case of a fraud. The bank should specifically indicate the period for which the guarantee is valid. The guarantee should also indicate the claim period, usually beyond the validity period of the guarantee.

(ii) *Before making payment under the bank guarantee* –The bank while making the payment under a guarantee has to ensure that the invocation is proper and that the person invoking the guarantee has the authority to invoke the guarantee. This should be clarified in the contract-agreement.

(c) In case of invocation, the banker is required to ensure that:

(a) The invocation is well within the claim period.

(b) The amount claimed by way of invocation is not in excess of what is guaranteed.

The authority invoking the guarantee has the powers to do so. In the case of Government Departments, the authority to invoke bank guarantee is usually placed in a position by way of delegation and allocation of authority. It is the duty of the banker is to ensure about the authority invoking the bank guarantee.

(d) The liability of the bank under a guarantee depends on:

(i) the amount of the guarantee and

(ii) the period of the guarantee

These two are important factors to be clearly mentioned in the guarantee issued by the banker, otherwise the bank's liability could be unlimited.

Pursuant to the amendment to section 28 of the Indian Contract Act 1872, the limitation period on a contract of guarantee cannot be restricted to less than the period provided under the limitation Act. As such if the guarantee is invoked in time the beneficiary can sue the bank within 30 years in case the beneficiary is a government or municipal body or 3 years in all others cases.

(e) Banks always specify the period for which their guarantee subsists and an additional period during which a claim has to be made on the bank to make payment. The former period during which the guarantee subsists is called the validity period and latter, the claim period. If any default has been committed by the debtor (i.e. the bank's customer) it should be within the validity period.

The bank should specifically indicate the period for which the guarantee is valid. The guarantee should also indicate the claim period, usually beyond the validity period. Invocation should have been made within the validity period. The claim period is usually a few months beyond the validity period of the guarantee and it is preferred to mention the exact period and time of grace.

(f) With effect from 1st January, 1987, Section 28 of Indian Contract Act had been amended. As a result of which the standard limitation clauses in the bank guarantees by which the banks extinguished their liability have been declared illegal. As such, at present, if a beneficiary is to invoke the guarantee within the claim period, for a default committed by the debtor during the validity period, then in case the bank does not make any payment, the beneficiary can sue the bank within the normal period as provided in the Limitation Act, 1963. This period under the Limitation Act is 30 years in case the beneficiary is a Government Department or Municipal Body and 3 years in all other cases.

(g) The bank while issuing a guarantee has to obtain counter guarantee from its customer and if necessary additional security and collateral to protect the bank in case it is required to pay under the guarantee. Though a bank guarantee is a contingent liability it is always prudent for a banker to secure this contingent liability in case it is enforced. This can be done by obtaining a counter guarantee cum indemnity executed by the customer in favour of the bank. The counter guarantee cum indemnity should be carefully drafted to ensure that in case the bank is to make payment on behalf of the customer, then the customer in turn should not only make good the amounts paid by the bank to the creditor but also any expenses connected therewith including costs of attorney, any interest on delayed payment, taxes and other levies. It is to take care of all the payments. The counter guarantee also includes an indemnity aspect. The counter guarantee should also include a clause that it would remain in force till the guarantee given by the bank subsists viz., till the bank is duly discharged by the beneficiary or a certificate to this effect is issued by the beneficiary.

(h) An injunction is an order issued by a court that forces the defendant – a person, a company, corporation or government entity – to do something or stop doing something, depending on what the plaintiff is requesting. In relatively rare cases, the court may issue a mandatory injunction, compelling a person, company, or government unit to take affirmative action in carrying out a specified action.

Injunctive relief is appropriate to prevent an action, to put a stop to ongoing or repeated conduct that violates a person's rights or causes injury, or to force a defendant to take action in order to prevent harm.

Question 2

(a) Kangana Tea Estate located in Dimapur district is a unit of Manisha Foods Ltd., Siliguri. The company operates in production and sale of fine quality Assam tea. Sanjay, aged 62 years, a long-time employee of the company, deals with day-to-day accounts function of Manisha Foods Ltd. You are the in-charge of treasury function of the company. You are on leave till another week from now, as there is a medical emergency, staying with your parents in a village that takes two days to reach from Siliguri.

Roshan, Managing Director of the company, is on an international business trip.

He received an SOS from the estate manager that there has been fire in the Tea Estate office building. Though there has been no casualty, more than 20 employees got injured while escaping out of the building and 24 employees have been hospitalised in a private nursing home located in the nearest town, about 45 kilometers from the estate office. Rescue work is still on.

You have received a call from Roshan, your MD, for ₹25 lakh to be made available to the Estate Manager at the earliest. He is not conversant with remittance of money through electronic mode by the bank.

Prepare a note for Roshan, giving details of the new age mechanism for transfer of funds electronically to enable him to issue suitable instructions to Sanjay. *(10 marks)*

(b) Comment on the following :

(i) The BASEL III accord deals in capital adequacy norms to be fulfilled by banks.

(ii) Mortgage by deposit of title deeds is called English mortgage.

(iii) Customer segmentation refers to classification of customers into different groups for the purpose of identifying their requirements.

(iv) Financing under micro finance is without collateral.

(v) Assignment is a term associated with loan against life insurance policy.

(vi) In case of pledge, possession remains with the borrower.

(vii) Nomination can also be done for home loans.

(viii) RBI is a banker to the government.

(ix) Tier-II capital shall not exceed 5O% of Tier-I capital.

(x) Commercial papers are issued at par value. *(2 marks each)*

Answer 2(a)

To

Mr. Roshan
Managing Director
Kangana Tea Estate

This is with reference to the various mechanisms for transfer of funds electronically. As a Manger-treasury functions, I would like to apprise you the various methods of transfer of funds electronically which are as follows:

(a) *Electronic Clearing System (ECS)* : ECS is a retail funds transfer system to effect payments (utility bills, dividends, interest, etc).ECS helps corporates, government departments, public sector undertakings, utility service providers to receive and/or pay bulk payments.

(b) *Real Time Gross Settlement (RTGS)* : RTGS is an electronic payment system, where payment instructions are processed on a 'continuous' or 'REAL TIME'

basis and settled on a 'GROSS' or 'individual' basis without netting the debits against credits. The payments so effected are 'final' and 'irrevocable'. The settlement is done in the books of the central bank (RBI). Both customers and banks can transfer fund monies the same day at regular intervals within the banking hours.

(c) *National Electronic Funds Transfer (NEFT)* : NEFT is a system similar to RTGS with some differences. Once the applicant for the transfer of funds furnishes full and correct details (correct details of account means correct name of the beneficiary, the account number, the branch and bank of the beneficiary, and the IFS code, etc.),funds can be transferred to the beneficiary's account by the remitting bank. Transfer of funds through NEFT is safe, quick. It reduces the paper work and is cost effective.

(d) *Internet Banking* : Internet banking is one of the popular e-banking modes has changed the banking operations and offer virtual banking services to the clients on 24 x 7 basis. It is also called as convenient banking, since the customer (account holder) can have access to his bank account from anywhere at any time, through the bank's web site. The customer is allowed online access to account details and payment and funds transfer facilities. Net banking services of a bank can be accessed through a Personal Identification Number (PIN) and access password as in the case of ATMs.

(e) *Core Banking Solutions (CBS)* : Core Banking Solutions has helped banks to offer better customer service. It has also reduced the cycle time of payment, mainly in clearing process and the process helped to achieve an increased efficiency. The Core Banking Solutions mainly work on the support of effective communication and good information technology. It is on account of merger of communication technology and information technology which enables the banks to offer core banking needs of the clients.

Mr. X
Manager- Treasury Function
Kangana Tea Estate

Answer 2(b)

(i) **This statement is true.** The BASEL III regulations based on three-mutually reinforcing Pillars viz. minimum capital requirements, supervisory review of capital adequacy and market discipline of BASEL II.

(ii) **This statement is False.** Mortgage by deposit of title deeds is called Equitable Mortgage.

(iii) **This statement is true.** It is the practice of classification of a customer base into groups of individuals that are similar in specific ways relevant to marketing, such as age, gender, interests and spending habits.

(iv) **This statement is true.** Financing under micro finance is without collateral. This is for very small amount for SHG (Self Help Group) comprising of very poor people and it is for social benefits.

(v) **This statement is true.** A borrower may assign any of the following items to secure a loan viz., (i) book debts (ii) life insurance policies (iii) money due from Government department.

(vi) **This statement is False.** Pledge can be created only in the case of existing goods (and not on future goods) which are in the possession of the pledger himself. It is for the physical presence of goods pledged.

(vii) **This statement is False.** Nomination cannot be done for home loans but in case of joint finance the survival has a right.

(viii) **This statement is true.** In terms of Sections 20 and 21 of the RBI Act 1934, the RBI has the obligation to transact the banking business of the Central Government.

(ix) **This statement is False.** Tier II capital shall not exceed 100 per cent of Tier I capital.

(x) **This statement is False.** Commercial papers are issued by companies with high credit ratings, in the form of promissory notes, at discount but repayable at par, to their holder at maturity.

Question 3

Why letters of credit and letters of guarantee issued by banks on behalf of their customers not shown in the balance sheet as advances are reported separately as off balance sheet items ? *(5 marks)*

Answer 3

Letter of Credits and Letter of Guarantees issued by banks on behalf of their customers are contingents which do not exist as on the date of balance sheet. There is no actual liability as the date of balance sheet but they may arise in future. Letter of credit is granted for future purchase of material expected to be received in due course of time and is not available physical in the unit premises.

Unlike other items, which are classified as balance sheet items, the contingent liabilities are classified as off balance sheet items. The balance sheet items are parts of the balance sheet as historical items, whereas the contingent liabilities are future items. In case these items become payable, it would affect the liquidity position of the company.

Question 4

Sunshine Ltd. is sanctioned ₹10 crore cash credit limit but utilises only ₹8 crore on an average at contracted rate of 20%. The borrower will have to pay a commitment fee @ 0.50% on the unused portion of the credit limit. Additionally, the bank insists for margin (cash deposit) of 20% of the utilised limit and 5% of the unutilised portion. Reserve requirement imposed by central bank is 10% of the deposits. In light of the above -

(i) What is the revenue from this loan to the bank ?

(ii) Work out estimated funds outlay for the borrower. *(5 marks)*

Answer 4

(i) Calculation of revenue from this loan to the bank

= Revenue from credit limit utilized + Revenues from credit limit unutilized

= Rs. 8 crores x 0.20 + Rs. 2 Crores x 0.005

= Rs. 1.61 crores

(ii) Calculation of funds outlay for the borrower

= Utilized Credit limit less (Margin requirement + Reserve requirement)

= Rs. 8 crore – (Rs. 8 crore x 0.20 + Rs. 2 crore x 0.05) – (Rs. 1.6 crore + Rs. 0.10 Crore) x 0.10

= 8-(1.60 +0.10) – (1.7 x 0.10)

= 8-1.70-0.17

= Rs. 6.13 crore

Alternate Method

Computation of funds outlay for the borrower	*Amount (Rs.)*
Cash outflow (net of margin@20%)	6,40,00,000
(8,00,00,000 x 80%)	
Less : Cash inflow from commitment	
Charges of unutilized limit	10,00,000
(2,00,00,000 x 5%)	6,30,00,000
Less : Margin requirement of RBI- @10% (on loan margin amount)	
10% of (8,00,00,000 x 20% + 5% x 2,00,00,000)	17,00,000
Or 10% of (1,60,00,000 + 10,00,000)	
Total funds outlay for the borrower	6,13,00,000

Question 5

Discuss salient features of the 'Banking Ombudsman Scheme'. On what grounds can a customer lodge a complaint of deficiency in service with respect to loans and advances to the Office of Banking Ombudsman ? *(5 marks)*

Answer 5

The Banking Ombudsman Scheme enables an expeditious and inexpensive forum to bank customers for resolution of complaints relating to certain services rendered by banks. This service is available for complaints against a bank's deficiency of service. A bank's customer can submit complaint against the deficiency in the service of the bank's branch and the bank as applicable, and if he does not receive a satisfactory response from the bank, he can approach Banking Ombudsman for further action. Banking Ombudsman is appointed by RBI under Banking Ombudsman Scheme, 2006. RBI as

per Section 35A of the Banking Regulation Act, 1949 introduced the Banking Ombudsman Scheme with effect from 1995.All Scheduled Commercial Banks, Regional Rural Banks and Scheduled Primary Co-operative Banks are covered under the Scheme.

As regards loans and advances, a customer can also lodge a complaint on the following grounds of deficiency in service with respect to loans and advances:-

– Non-observance of Reserve Bank Directives on interest rates; delays in sanction, disbursement or non-observance of prescribed time schedule for disposal of loan applications;

– Non-acceptance of application for loans without furnishing valid reasons to the applicant; non-adherence to the provisions of the fair practices code for lenders as adopted by the bank or Code of Bank's Commitment to Customers, as the case may be.

Example : Mr X deposited a bank draft in his account but it was not credited to his account. After several reminder and communication to bank authorities at different level the problem was not sorted out. He decided to take shelter of judiciary but a bank manager advised him to contact the Ombudsman of banking. He did so with all documents. Within 10 days a decision was taken and he was paid the principal with 3 months interest.

Question 6

Neelima opened a savings bank account with Dhan Bank. She was handed over a copy of rules and regulations for operating the account. It provided that the cheque book should be kept under lock and key and for loss, if any, arising from not complying with requirement, the bank will not be responsible.

Neelima kept the cheque book in drawer and one of her office colleagues took off one cheque leaf and by forging her signature withdrew ₹2 lakh from the bank. She claimed refund of this amount from the bank. Bank refused to pay stating that the loss has been caused due to negligence on part of the customer. She has filed an appeal against the bank.

Give your decision on the case with reasons. *(5 marks)*

Answer 6

In general terms, if someone forges a signature on a cheque, the person whose signature was forged is not bound to honor the cheque, and their bank does not have to pay it. A cheque with a forged signature is simply a worthless piece of paper – a "nullity".

In this case, if Dhan bank pays out on the basis of a forged signature on a cheque, it does so without Neelima's mandate and is required to make good any loss that the payment causes Neelima. It does not matter how good the forgery is; a skillful forgery is no more valid than a crude one. Dhan Bank is liable for payment of a forged cheque and will have to restore the amount to the credit of the account.

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CAPITAL, COMMODITY AND MONEY MARKET

(Elective Paper 9.2)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Rise Ltd., a listed company having registered office in Delhi, has proposed two financial plans. Details of the same are given below :

Sources of funds	*Plan - 1*	*Plan - 2*
Equity shares of ₹100 each	*₹22,50,000*	*₹45,00,000*
12% Preference shares of ₹100 each	*₹50,00,000*	*Nil*
Debentures (convertible after 2 years)	*₹10,00,000 @10% interest*	*₹30,00,000 @ 10% interest*
Tax rate	*35%*	*35%*

You are required to answer the following -

(a) Compute :

(i) Two EBIT-EPS co-ordinates for each plan, assuming expected EBIT ₹25,00,000. (10 marks)

(ii) Indifference point. (5 marks)

(iii) Financial break-even point for each plan. (5 marks)

(b) Explain which financial plan is more risky out of the above two plans and why ? (5 marks)

(c) Find out the EBIT range in which one plan is better than the other plan. (5 marks)

(d) Recommend the plan if Rise Ltd. is fairly certain that its EBIT will be ₹25,00,000. Give reasons. (5 marks)

(e) Prepare verification table for the above. (5 marks)

(f) List out the advantages of convertible debentures for the company and to its investors. (5 marks)

(g) Explain the conditions for private placement of, non-convertible redeemable preference shares. (5 marks)

Answer 1(a)(i)

EBIT-EPS co-ordinates for each financial plan

	Plan-1	*Plan-2*
Interest on debentures	Rs. 1,00,000	Rs. 3,30,000
Dividend on preference shares Before taxes 600000/(1-0.35)	Rs. 9,23,077	NIL
	Rs. 10,23,077	Rs. 3,30,000

	Plan-1	*Plan-2*
Expected EBIT (Rs.)	25,00,000	25,00,000
Less Interest on Debentures (Rs.)	1,00,000	3,30,000
Equity before tax (Rs.)	24,00,000	21,70,000
Less Taxes (Rs.)	8,40,000	7,59,500
Earnings after tax (Rs.)	15,60,000	14,10,500
Less pref. Share dividend (Rs.)	6,00,000	NIL
Earning for equity shares (Rs.)	9,60,000	14,10,500
Number of shares	22,500	45,000
EPS (Rs.)	42.67	31.34

Co-ordinates	***EBIT financial plan***		***EPS financial plan***	
	Plan-1	*Plan-2*	*Plan-1*	*Plan-2*
Lower (one)	10,23,077	3,30,000	Zero	Zero
Higher (two)	25,00,000	25,00,000	42.67	31.34

Answer 1(a)(ii)

Indifference Point

Let the Expected EBIT be X

Equation for Plan 1 [(X-1,00,000)x0.65 - 6,00,000]/22500

Equation for Plan 2 [(X-3,30,000)x0.65]/45000

Both equation **must be equal** to find out indifference point

$$\frac{(X - 1,00,000) \times 0.65 - 6,00,000}{22500} = \frac{(X - 3,30,000) \times 0.65}{45000}$$

$$\frac{0.65X - 65,000 - 6,00,000}{22500} = \frac{(0.65\ X - 2,14,500)}{45000}$$

Cross multiplication for solving equation:

[0.65X - 6,65,000x45000 = [0.65X-2,14,500]x22,500

29,250 X-29,92,50,00,000 = 14625X-4,82,62,50,000

29250 X-14625X = 29,92,50,00,000 - 4,82,62,50,000

14,625 X = 25,09,87,50,000

$$X = \frac{25,09,87,50,000}{14,625}$$

= 17,16,154

Hence indifference point be Rs. 17,16,154

Answer 1(a)(iii)

Financial Breakeven point of each plan

Plan 1- Rs. 10,23,077

Plan 2- Rs. 3,30,000

Answer 1(b)

Plan-1 has more financial risk as its DFL is likely to be higher.

Plan-1 has higher Debt to Equity ratio as compared to Plan-2.

Therefore, Plan-1 is more risky than Plan-2.

Debt/Equity Ratio (Plan-1) = 60,00,000/22,50,000 = 2.66

Debt/Equity Ratio (Plan-2) = 30,00,000/45,00,000 = 0.66

Answer 1(c)

Plan-2 is better for EBIT Level of less than Rs. 17,16,154. Plan-1 is better for EBIT ranges beyond that level.

Answer 1(d)

Plan-1 is better as EPS will be higher. The EPS calculation if reflected below:

	Plan-1	**Plan-2**
Expected EBIT (Rs.)	25,00,000	25,00,000
Less Interest on Debentures (Rs.)	1,00,000	3,30,000
Equity before tax (Rs.)	24,00,000	21,70,000
Less Taxes (Rs.)	8,40,000	7,59,500

Earnings after tax (Rs.)	15,60,000	14,10,500
Less pref. Share dividend (Rs.)	6,00,000	NIL
Earning for equity shares (Rs.)	9,60,000	14,10,500
Number of shares	22,500	45,000
EPS (Rs.)	42.67	31.34

Answer 1(e)

	Plan-1	**Plan-2**
Expected EBIT (Rs.)	17,16,154	17,16,154
Less Interest on Debentures (Rs.)	1,00,000	3,30,000
Equity before tax (Rs.)	16,16,154	13,86,154
Less Taxes (Rs.)	5,65,654	4,85,154
Earnings after tax (Rs.)	10,50,500	9,01,000
Less pref. Share dividend (Rs.)	6,00,000	NIL
Earning for equity shares (Rs.)	4,50,500	9,01,000
Number of shares	22,500	45,000
EPS (Rs.)	20,02	20,02

Alternate Answer 1(e)

	Plan-1	**Plan-2**
Expected EBIT (Rs.)	25,00,000	25,00,000
Less Interest on Debentures (Rs.)	1,00,000	3,30,000
Equity before tax (Rs.)	24,00,000	21,70,000
Less Taxes (Rs.)	8,40,000	7,59,500
Earnings after tax (Rs.)	15,60,000	14,10,500
Less pref. Share dividend (Rs.)	6,00,000	NIL
Earning for equity shares (Rs.)	9,60,000	14,10,500
Number of shares	22,500	45,000
EPS (Rs.)	42.67	31.34

Answer 1(f)

The advantages of convertible debentures to the company are –

1. Capitalisation of interest cost till the date of commissioning of the project is allowed.

2. Lower interest as compared to the rate charged by the Banks and Financial Institutions.
3. Debentures is treated as equity for computing the debt equity ratio.
4. Equity capital gets increased after each conversion.
5. Tax benefits are higher.
6. Popular form of financing.
7. Greater degree of autonomy for the companies.

The advantages of the convertible debentures to the investors are –

1. Fixed return till conversion
2. Investor gets value appreciation
3. Debentures generally carry security with a charge on all or a part of movable/ immovable properties of the company. This assures prompt payment of principal and interest by invoking the assistance of a debenture trustee.

   However in terms of SEBI Regulations where the debentures have a maturity period of 18 months or less it is mandatory for the company to create security on the debentures.
4. A fair amount of liquidity is enjoyed by convertible debentures listed on the stock exchanges depending on the track record of the companies. Even if debentures are not traded as actively as equity shares, convertible debentures of good companies command reasonable liquidity. Where a debenture has several parts, each part of the convertible debentures can be traded separately or in full on the stock exchanges.
5. The following options are available to the investor who has bought convertible debentures issued in several parts:
   (a) To sell all the parts immediately on allotment;
   (b) To sell one or more parts and retain other or others till conversion and to obtain equity shares for retention or sale.

Answer 1(g)

Conditions for Private Placement of non-convertible redeemable preference shares

1. An issue may list its non-convertible redeemable preference shares (NCRPS) issued on private placement basis on a recognized stock exchange subject to the following conditions:
   (a) In compliance with the provisions of the Companies Act, 2013, rules prescribed there under and other applicable laws;
   (b) Credit rating has been obtained from at least one credit rating agency registered with SEBI;
   (c) Should be in dematerialized form;

(d) The disclosures as provided in regulation have been made;

(e) The minimum application size for each investor is not less than 2 lakh rupees; and

(f) Where the application is made to more than one recognized stock exchange, the issuer shall choose one of them as the designated stock exchange.

2. The issuer shall comply with conditions of listing of such non-convertible redeemable preference shares as specified in the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 where such non-convertible redeemable preference shares are sought to be listed.

3. The issuer making a private placement of non-convertible redeemable preference shares and seeking listing thereof on a recognized stock exchange shall make disclosures as specified in Schedule I of SEBI (Issue and Listing of Non-convertible Redeemable Preference Shares) Regulations, 2013 accompanied by the latest Annual Report of the issuer.

4. The disclosures as required in point 3 above shall be made on the websites of stock exchanges where such securities are proposed to be listed and shall be available for download in PDF/HTML formats.

Question 2

(a) Clory Ltd. is a listed company with :

— *Authorised capital of 500 crore (i.e., 50 crore equity shares of ₹10 each); and*

— *Fully paid-up equity share capital of ₹200 crore.*

Glory Ltd. is now making equity issue of balance capital, i.e., for 30 crore shares of ₹10 each under qualified institutional placement (QIP). The receipt of funds on account of applications and present status are as follows :

(i) There are 4 (four) available qualified institutional buyers (QIBs) including mutual funds who have deposited the amount upto the amount of issue.

(ii) Out of QIBs as mentioned in (i) above, one QIB is willing to buy 51% of the said issue, i.e., for ₹153 crore for better exercise of control. The other three investors are not related/associated with the former.

(iii) Out of IBs as mentioned in (i) above, one QIB is still not satisfied with the performance of the company and has written that they may be given an opportunity to withdraw 50% of the application money after the closure of issue.

(iv) The issue is made with optionally convertible instruments and exchangeable with equity shares up to 7 years (i.e.,84 months).

(v) The allotment is being made in the 13th month after passing the shareholders' special resolution and it is explained by the company that there was delay in negotiation with QIBs for investment and the delay is beyond the control of the company and cause is external one.

The issue is within the prescribed limit of the pre-issue net worth and it is

intended for enlistment as a further issue with the stock exchange where it is listed. As a Practising Company Secretary engaged by Glory Ltd., advise the company keeping in view the situations mentioned in points (i) to (v) above, with reasons. *(10 marks)*

(b) *Foreign currency convertible bonds (FCCBs) and foreign currency exchangeable bonds (FCEBs) are both aimed at to finance business of Indian companies, but the two are quite different in methodology.*

Bring out the similarities and distinctions between the two type of bonds. *(10 marks)*

(c) *Kite Ltd. is a public company which intends to get its equity shares listed at BSE. Kite Ltd. has approached you to advise about the conditions of listing regulations with respect to maintenance of mandatory functional website by every listed entity.*

Give your advice to Kite Ltd. about the specific requirements mentioning the relevant provisions of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. *(10 marks)*

Answer 2(a)(i)

The minimum required number of allottee must be 5 (Five) for issue size above Rs. 250 Cr. In the given case only 4 (four) number of QIB including mutual fund has deposited amount, hence this is not in order.

Answer 2(a)(ii)

An allottee can apply maximum up to 50% of the issue size, so it is not a valid proposition, he has to restrict application for equity up to Rs. 150 crores in value.

Answer 2(a)(iii)

The applicant in QIP category, cannot withdraw their bid whether in full or part after closure of the issue.

Answer 2(a)(iv)

The maximum tenure of convertible instrument is 60 months. Hence, in the instant case proposal for 7 (seven) years is not permissible.

Answer 2(a)(v)

The life of the special resolution is valid for 1 year from the date of AGM/EGM. The company is required to have fresh approval once again. The old resolution shall not be valid after one year. The pleading/argument of company are not tenable.

Answer 2(b)

The similarities between FCCB and FCEB are given below:

1. Both are issued by Indian Companies.
2. Both Bonds are denominated in foreign currency.
3. Principal and interest payable in foreign currency, if not converted in equity shares-as the case may be.

4. Maturity of Bonds not less than 5 (Five) years.

Difference between FCCB and FCEB are given below:

S.No.	*FCCB's*	*FCEB's*
(i)	Optionally convertible into fixed number of equity shares of Indian issuer company, or take maturity value with interest.	Exchangeable partly or fully into equity shares of promoter group company, known as "Offered Company" [O.C].
(ii)	25% of proceeds can be used for general corporate restructuring.	No such clause are applicable.
(iii)	If the conversion is in favour of the Bond holder as per prevailing price of equity shares of the issuer in Indian market, then conversion is preferable other-wise take back majority value & interest.	Wholly or partially convertible into the shares of the "Offered Company (O.C)"- not the issue company.
(iv)	It involves two parties- (i) Indian issuer company, (ii) Person resident outside Indian-investor.	It involves at least 3 parties- (i) Issuer Indian company, (ii) Offered Company (O.C), (iii) Investor-resident outside India.
(v)	Issue of attached warrant are not permitted.	Warrant can be attached in this instrument.
(vi)	One Indian company alone can issue and implement.	Only a member company of a group of companies can only do so and implement.
(vii)	It is simplest	It is a bit complex procedure.

Answer 2(c)

Regulation 46 to SEBI (Listing Obligation and Disclosure Requirements) Regulation, 2015 requires following:

Mandatory to maintain functional website : It is mandatory for the listed entity to maintain a functional website containing the basic information about the listed entity.

A. *Dissemination of Information at website the company :* The following information are required to be disseminated on the website of the company.

1. Details of its business;
2. Terms and conditions of appointment of independent directors;
3. Composition of various committees of Board of Directors;
4. Code of conduct of board of directors and senior management personnel;

5. Details of establishment of vigil mechanism/WBP
6. Criteria of making payments to non-executive directors, if the same has not been disclosed in annual report
7. Policy on dealing with related party transactions;
8. Policy for determining 'material' subsidiaries;
9. Details of familiarization programmes imparted to independent directors;
10. The email address for grievance redressal and other relevant details;
11. Contact information of the designated officials of the listed entity who are responsible for assisting and handling investor grievances;
12. Shareholding Pattern;
13. Financial results;
14. Details of agreements with media companies, analysts etc.

B. *The listed entity shall*

— Ensure that the contents of the website are correct;

— Update any change in the content of its website within two working days from the date of such change in content.

Question 3

Under the Depositories Act, 1996, the depository facilitates its beneficiary account holders to create a pledge or hypothecation in favour of another person/entity, who also has a beneficiary owner's (B.O.) account.

Neeraj has a B.O. account and wishes to create pledge against holding of some equity shares in favour of another person who will provide him loan. However, he is confused to differentiate between 'pledge' and 'hypothecation'. Neeraj approached you as a Company Secretary in Practice to understand the difference between the two and which is safer for him.

Advise Neeraj referring to the relevant provisions of the Depositories Act, 1996.

(5 marks)

Answer 3

(i) In case of pledge created/made by a pledger and the pledge contains a unilateral/ unfettered right to appropriate such asset without taking any consent from the pledger in case of default made/committed by the pledger.

(ii) On the other hand, if the lender/pledge requires consent/concurrence of the pledger for appropriation of securities, whether full or part, is then called as HYPOTHECATION.

(iii) The pledge heavily favours the lender (pledgee), whereas hypothecation is safer to the borrower (pledger).

(iv) The Depository Act permits the creation of pledge/hypothecation on free securities through its beneficiary owners (B.O) account. The both parties must have B.O account under the one depository, however it need not under the same participant (i.e. D.P).

Question 4

Meera Ltd. has 50,000 fully paid-up equity shares as on 31st March, 2016. The shareholding pattern of Meera Ltd. is given below :

	No. of Shares
Shares held by founders/directors/acquirers - who can exercise control	*21,000*
Shares held by partner with controlling interest	*3,000*
Holding of shares through FDI	*2,000*
Independent public companies	*4,000*
Strategic stakes by corporate bodies	*3,000*
Cross holding by group/associate companies	*1,000*
Lock-in-shares which would not be sold in open market	*2,000*
Retail investors	*13,000*
Employees' welfare trust	*1,000*
TOTAL	*50.000*

You are required to -

(a) Define 'free float' and 'free float market capitalisation'. (2 marks)

(b) Compute the free float of the company and its percentage to the total equity shares based on the above facts. (3 marks)

Answer 4(a)

(i) *Free float* is a term in stocks trading. It describes the proportion of shares of a publicly traded company that is traded in the stock market. Note that not all free float shares may be actively circulating on the market at any given time as many traders purchase shares as a long-term investment.

(ii) *Free-float market capitalization* takes into consideration only those shares issued by the company that are readily available for trading in the market.

— it generally excludes

— promoters' holding

— government holding

— strategic holding and

— other locked-in shares that will not come to the market for trading in the normal course.

In other words, the market capitalization of each company in a Free-float index is reduced to the extent of its readily available shares in the market.

Answer 4(b)

Computation of Free Float of MIPL

Shares held by Independent Public Corporate	4,000 shares
Shares held by Retail Investors	13,000 shares
Total Shares under free float category	17,000 shares
% of total shareholding	[17000/50,000] x 100 = 34%

Question 5

Illustrate the difference between 'money market' and 'capital market'. *(5 marks)*

Answer 5

Distinguish between money market and capital market

Money Market	*Capital Market*
1. Lending or borrowing of short-term, one year or below	1. Lending borrowing of short-term more than one year
2. Call Money,Treasury Bills, Commercial Bills, Commercial Papers, and Bills of Exchange	2. Stocks, Shares, Debentures, Bonds, Corporate Deposits
3. Commercial banks, acceptance houses, non-banking financial institutions, bill brokers	3. Stock exchanges, banks, insurance, mortgage banks
4. Provides working capital	4. Provides capital to buy land machinery
5. Low risk and high liquidity	5. High risk and low liquidity
6. Central bank has close and direct link	6. Central bank indirect link
7. Commercial bank are closely regulated	7. Institutions are not much regulated

Question 6

"For the purpose of prevention of misuse of 'price sensitive information' all the directors/ officers and designated employees will have to work under a restricted mechanism and environment." Discuss. *(5 marks)*

Answer 6

In line with the requirement of SEBI (Prohibition of Insider Trading) Regulation, 2015 certain restrictions are imposed on officials of the company to prohibit insider trading in the scrip of the company on the basis of possession of unpublished price sensitive information.

Chapter – II of the SEBI (PIT) Regulation, 2015 discusses the restrictions on

communication and trading by the Insiders. A consolidated study of section, 4, 5 and even 6 directs a comprehensive mechanism for regulating the conduct of the employees, directors and officers in possession of undisclosed price sensitive information. The entire process can be briefed under the three heads below:

1. *Disclosure* : Typically, disclosure is mandated at two levels;

   - One is the immediate disclosure of any material information and
   - The other is the disclosure of transactions undertaken.

   While the former is meant to prevent insider trading, the latter is for revealing insider trading, if any. Insiders and the company are obligated to disclose all the price sensitive/ material information to the public at the earliest so that a level playing field is achieved amongst all the shareholders and proposed investors. When the information is equally available to all, there is no distinct advantage that insiders can capitalize on.

2. *Trading Restrictions (Closing of Trading Window)* : Insiders may be restricted from dealing in the securities, directly or indirectly, during certain specific time periods to stop them from taking advantage of having the material information before the public or the other shareholders. It goes without saying that, the insiders are prohibited from dealing in securities when they are in possession of or have access to material non-public information. Additionally, insiders may also be prohibited from dealing in securities for a certain period after the information is disclosed to the public. The insiders can place the buy/ sell orders simultaneously with the disclosure of information or immediately thereafter. In that event, insider trading would have happened in that very short spell between the disclosure of information and the public reaction to it. Though, technically this may constitute insider trading, the insiders are still exploiting their access to information to touch the finish line before others. Therefore, the trading window should remain shut for the insiders for a certain period immediately after the disclosure of the material information. This will ensure effective dissemination of the disclosed material information before the insiders jump into action. A stricter measure would be permitting insiders to deal in the securities only through a specifically designated trading window that is controlled and monitored by the company or the stock exchange.

3. *Pre-clearance of Trades* : A condition may be imposed on the insiders that they can deal in the securities of the company only after obtaining a prior approval in accordance with the procedure and policy prescribed by the company in that regard. In addition, it may also be prescribed that a pre-approved trade will have to be undertaken within the stipulated time period, failing which the approval would lapse.

Contravention of provisions of SEBI (PIT) Regulations, 2015 is a punishable offence under SEBI Act, 1992.

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INSURANCE LAW AND PRACTICE

(Elective Paper 9.3)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Kishore, owner of Jeevan Brothers, a business enterprise, had taken two insurance policies from a general insurance company on his factory located in Goa. One was a fire policy and the other was a consequential loss of profit due to fire policy.

On 8th January, 2015, early morning around 3.00 A.M., there was a short-circuit in the main switch-board in the sub-station receiving power from the State Electricity Board which resulted in a flashover producing over-currents. The flashover and over-currents generated excessive heat which caused the paint on the panel board to be charred, producing smoke and soot thereby causing a hole to develop in the adjoining feeder. The smoke and soot alongwith the ionized air travelled to the generator compartment where again a short-circuit took place resulting in the tripping of the generator. This resulted in the entire power supply to the plant being stopped and due to this, the supply of water/steam to the waste-heat-boiler by the flue gases at a high temperature continued to be fed into the boiler resulting in damage to it.

Kishore had the losses examined which were calculated at :

(i) ₹1,35,17,709 for material loss due to damage to the boiler and other connected equipments; and

(ii) ₹19,11,10,000 as loss of profits for the period during which the plant had to be shut down due to the accident.

He had intimated the insurance company of the accident and loss in due time and subsequently made a claim under the two policies on the insurer. He had sent alongwith the claim, the surveyors' reports. The insurance company rejected the claim holding that the loss did not occur due to fire. Hence, Kishore took tie matter to the National Commission under the Consumer Protection Act, 1986.

Before the National Commission, the insurance company reiterated its stand that the damage to the boiler and other equipments was not caused by fire but because of stoppage of electricity due to short-circuit in the switch-board, resulting in stoppage of power leading to a thermal shock. It started that the proximate cause had to be seen for settling a fire claim which in the present case was the thermal shock due to stoppage of power. The National Commission, on examination of the facts, did not agree to the insurer's arguments and decided in favour of Kishore.

The insurer not satisfied with the National Commission's decision carried the matter further to a legal forum where again the counsel laid stress on two issues, viz., (a) there was no fire; and (b) in any case, fire was not the proximate cause for the damage.

The counsel for the insured relied on the decision of the National Commission and

argued that it was necessary to determine first whether there was a fire. Admittedly in this case, there was a short-circuit causing a flashover. A flashover is the near simultaneous ignition of all combustible material in an enclosed area. When certain materials are heated, they undergo thermal decomposition and release flammable gases. Flashover occurs when the majority of surface in a space is heated to the auto-ignition temperature of flammable gases. In the present case, it was noticed that the short-circuit in the main switch board caused a flashover. According to one of the two surveyors, this flashover should be defined as a phenomenon of a developing fire (or radiant heat source), radiant energy at wall and ceiling surfaces within a compartment. In the present case, ihe paint.got burnt due to the flashover and such high energy levels would, undoubtedly, result in a fre causing melting of the panel board.

The second surveyor admitted that fire of a short duration could not be called a 'sustained' fire as contemplated by the insurer. In his view, the duration of fire was not at all relevant so long as there was a fire causing damage to the asset. The claim was maintainable even if the fire was for a fraction of a second. The counsel reiterated that the term 'fire' in the fire policy was not qualified by the word 'sustained' and the Appellate Court should bear in mind the basic proposition of law that a court should not add words to the statute or to a document and the policy must be read as it was. The counsel, therefore, stated that the insurance company's argument that there was no 'sustained' fire in this case and hence the claims were not admissible was basically incorrect and wrong.

The Court after hearing both the parties agreed to the argument that what was to be decided in this case, whether the loss to the property was caused by 'fire' and not 'sustained' fire. It had been clearly established in the case and also supported by the reports of the two surveyors that there was a flashover in this case resulting in a fire of whatever limited time that had caused the blackening of the switch-board and the consequent loss to the boiler and other equipments. Had the fire not occurred, the damage would not have occurred and that there was no intervening agency that was an independent source of the damage to the plant.

The Court also referred to the decision in General Assurance Society Ltd. v. Chandmull Jain and another [AIR 1966 SC 1644] where it was laid down by the Constitution Bench that in case of ambiguity in a contract of insurance, the ambiguity should be resolved in favour of the insured and against the insurance company.

The insurer had not questioned the quantifications of losses by the surveyors. The Court, therefore, felt that the claims under the two policies were allowable in favour of Kishore and consequently dismissed the insurance company's appeal.

On the basis of the above facts and information, answer the following questions -

(a) Is the insurance company justified in rejecting the claim ? What are your views on Kishore's claims ? (7 marks)

(b) Define 'fire' and how do you recognise the existence of fire. Relate your answer with the facts of the above case. (7 marks)

(c) What is 'proximate cause' and its relevance ? Determine the proximate cause in the above case. (8 marks)

(d) In case of ambiguity in a contract of insurance, it should be resolved in favour of

the insured. Discuss the relevant provisions in a their applicability to the above case. *(8 marks)*

(e) Define 'fire insurance' and explain the risks covered and exclusions under a standard fire and special perils policy. *(10 marks)*

(f) Is it compulsory for a loss to be surveyed by a person ? Who can conduct such a survey and what are the duties of such a surveyor ? *(10 marks)*

Answer 1(a)

In the present case, on perusing the facts it is very clearly seen that the insurance company was not justified in refusing to pay the claims, since the reasons for the loss was very much covered by the terms and conditions of the policy. On the other hand, the claim made by Kishore was genuine and had to pay. As seen from the case details, the loss was caused due to short circuit circulating which resulted in a flash over. The cause of loss to the boiler and equipment was due to the fire. Short circuit circulating resulted in a flash over. Due to this flash over and over currents, excessive heat energy was generated which resulted in the evolution of marginal fire. The surveyors observed in their reports that a flash over took place. Fire of an extremely short duration followed short circuit. Due to this flash over and over currents, excessive heat energy was generated which resulted in the evolution of marginal fire. As fire was the proximate cause of the loss, the claim was genuine and stand taken by insurance company was not tenable.

One of the basic principles of insurance is Principle of Causa Proxima. Principle of Causa Proxima, or in simple English words, the Principle of Proximate (i.e Nearest) Cause, means when a loss is caused by more than one causes, the proximate or the nearest or the closest cause should be taken into consideration to decide the liability of the insurer.

Answer 1(b)

The meaning of 'Fire' is Ignition under accidental circumstances. Essentials of proof ofa fire include firstly there should be an actual ignition of the property which ought not to have been on fire, under accidental circumstances. Basically Fire Insurance Policies are designed to provide protection against material loss or damage, by fire and other specified perils. Fire or combustion is result of normally fuel, oxygen initial source ofheat. In the present case, the loss was evidently caused by "Flashover, which can be defined as a phenomenon of a developing fire (or radiant heat source) radiant energy at wall and ceiling surfaces within a compartment.

In the present case, the paint had been bumt due to the said flashover. Such high energy levels, would undoubtedly, have resulted in a fire, causing melting ofthe panel board." Hence the loss was evidently caused by fire.

Answer 1(c)

Proximate Cause can be defined as a cause which is not the cause that is nearest in time or place but the active and effective cause that sets in motion a chain of events which brings about the ultimate result without the intervention ol any other force working from an independent source. However, the question always is: Is the unbroken connection between the wrongful act and the injury, a continuous operation? In other words, did the

facts constitute a continuous succession of events, so linked together as to make a natural whole, or there was some new and independent cause intervening between the wrong and the injury. In the present case, if the proximate cause of the loss or destruction, including other machines, apparatus, fixtures, fittings etc, or part of the electrical installation is due to hre which started in an electrical machine or apparatus, all such losses is covered by the policy. The question is to test whether a flashover and fire was the proximate cause of the damage.

To understand this it is necessary to understand the sequence of events, which is as follows:

— Short-circuit takes place in the main switchboard receiving electricity from the State Electricity Board possibly due to the entry of a Verrnin.

— Short-circuit results in a flashover.

— Short- circuit and flashover produced over-currents, which in tum produced enormous heat.

— The over currents and the heat produced resulted in the expansion and ionization of the surrounding air. The electricity supply from the State Electricity Board got tripped.

— The paint ofthe Panel Board was charred by the enormous heat produced and the MS partition of the adjoining feeder connected to the generator power developed a hole.

— It resulted in formation of smoke/soot and the ionized air crossed over the MS partition and entered into the compartment receiving electricity from the generator. Consequently the generator power supply also got tripped.

— The tripling of purchased power and generator power resulted in stoppage of water/steam in the waste heat boiler.

— The Flue gases at high temperature continued to enter the boiler, which resulted in thermal shock causing damage to the boiler tubes.

In this connection, it may be noted that in their written submission belore the National Commission the company has admitted that there was a flashover and fire. Hence fire is the proximate cause of loss.

Answer 1(d)

"Adhesion" is a silent feature of insurance contract. In a contract of adhesion, one party draws up the contract in its entirety and presents it to the other party on a 'take it or leave it' basis; the receiving party does not have the option of negotiating, revising, or deleting any part or provision of the document. Insurance contracts are of this type, because the insurer writes the contract and the insured either 'adheres'to it or is denied coverage. In a court of law, when legal determinations must be made because of ambiguity in a contract of adhesion, the court will render its interpretation against the party that wrote the contract. Typically, the court will grant any reasonable expectation on the part of the insured (or his or her beneficiaries) arising from an insurer-prepared contract.

The above statement refers to the interpretation of the policy conditions and provisions.

As a matter of fact, in a policy, the wordings are very technical and not easy to understand. Therefore, law and guidelines very specifically emphasize using simple, understandable and clear language so that there is no confusion in understanding of the conditions by either party to the contract. In the present given case, there was a dispute with regards to the cause of loss. While the insured claimed that cause of loss is a covered cause of loss and hence the claim was not tenable. The surveyors accepted in their report that the cause of loss was not a sustained fire, but a possible fire after the flash over being of a very short duration. This means that they have also accepted the cause of loss to be fire but for a short duration. As the fire insurance policy conditions cover fire and as there was no mention ofa sustained fire in the policy wording, the insurance company cannot change the statutory definition and hence, as per law, and as per the doctrine of contra proferentum, the law clearly states that in any condition, in case there is any ambiguity in the policy, in a contract of insurance, the ambiguity should be resolved in favour of the claimant and against the insurance company. Therefore in the present case, the repudiation ofthe company was notjustified and hence the claim is payable and the dismissal of the case was also justified.

Answer 1(e)

According to Section 2 of the Indian Insurance Act, 1938, "Fire Insurance Business" is defined as 'the business of effecting, otherwise than incidentally to some other class of insurance business, contracts of insurance against loss by or incidental to fire or other occurrence customarily included among the risks insured in fire insurance policies.'

A Standard fire and Special perils policy covers the following 12 different types of risks covered such as Fire, lighting, Explosion/Implosion, Aircraft damage, Riot, Strike, Malicious and Terrorism damage (RSMTD), Storm, Cyclone, Typhoon, Tempest, Hurricane, Tomado, Flood and Inundation, Impact damage by rail/road/vehicle or animal, Subsidence and landslide (including rockslide) Bursting and./or overflowing of water tanks, apparatus and pipes, Missile testing operations, Leakage from automatic sprinkler installations, Bush fire etc.

The exclusions under a fire policy are:

— Loss of or damage to any electrical machine, apparatus, fixture or fitting (including electric fans, electric household or domestic appliances, wireless sets, televisions sets and radios) or to any portion of the electrical installation, arising from or occasioned by over running, excessive pressure short circuit, arcing selfheating or leakage of electricity from whatever cause(lightning included), provided that this exemption shall apply to the particular electrical machine apparatus, fixtures, fittings or portion of the electrical installation so affected and not to other machines, apparatus, fixture, fittings or portion of the electrical installation which may be destroyed or damaged by fire so set up.

— A perusal of the exclusion clause shows that the main part of the exclusion clause which protects the insurer from liability under the policy, covers loss of damage to any electrical machinery, apparatus, fixture or fittings including wireless sets, television sets, radio and so on which themselves are a total loss or a damage or damaged due to short circulating, arcing, self-heating or leakage of electricity. However, the proviso to the said clause through inclusion ofany other machinery, apparatus, fixture or fitting being destroyed or damaged by fire

which has affected any other appliances such as television sets, radio, etc. or electrical machines or apparatus are clearly included within scope of the fire policy for whatever damage or destruction caused by the fire. If for example the short circulating results in damage to a television set through fire created by the short circuiting in it, the claim for it is excluded under the fire policy. However, if from the same fire there is a damage, to the rest of the house or other appliances, the same is included within the scope ofthe fire policy by virtue of the proviso.

Answer 1(f)

No. It is not mandatory for an insurer to appoint a surveyor for each and every loss reported by a policy of general insurance. Only where the estimated loss exceeds Rs. 20,000, the insurers are mandated to appoint a licensed surveyor to assess and settle the loss. [Section 64UM (2) ofthe Insurance Act]

Every person who is an individual and intending to act as a surveyor and loss assessor in respect of general insurance business shall apply to the Authority for grant of license in FORM-IRDA-I-AF as given in the Schedule to these regulations. The Authority shall, before granting license. take into consideration all matters relating to the duties, responsibilities and functions of surveyor and loss assessor and satisfy itself that the applicant is a fit and proper person to be granted a license. In particular and without prejudice to the foregoing, the Authority shall satisfu itself that the applicant, in addition to submitting the application complete in all respects:-

(a) satisfies all the applicable requirements of section 64UM read with section 42D of the Act and rule 56A ofthe Insurance Rules, 1939;

(b) possesses such additional technical qualifications as may be specified by the Authority from time to time;

(c) has fumished evidence ofpayment of fees for grant of license, depending upon the categorization;

(d) has undergone a period of practical training, not exceeding 12 months, as contained in Chapter VII ofthese regulations; and

(e) fumishes such additional information as may be required by the Authority from time to time.

The Authority on being satisfied that the applicant is eligible for grant of license, shall grant the same in FORM-IRDA-2-LF as given in the Schedule to these regulations and send an intimation to the applicant together with an identity card mentioning the particular class or category of general insurance business namely, fire, marine cargo, marine hull, engineering, motor, miscellaneous and loss of profit for which the Authority has granted license and the license shall remain valid lor a period of five years from the date of issue thereof, unless cancelled earlier.

Some of the Obligation/Duties/Responsibilities of a Surveyor are:

(i) declaring whether he has any interest in the subject-matter in question or whether it pertains to any ofhis relatives, business partners or through material shareholding;

(ii) maintaining confidentiality and neutrality without jeopardizing the tiability of the insurer and claim of the insured:

(iii) conducting inspection and re-inspection of the property in question suffering a loss;

(iv) examining, inquiring, investigating, verifying and checking upon the causes and the circumstances of the loss in question including extent ofloss, nature of ownership and insurable interest;

(v) conducting spot and final surveys, as and when necessary and comment upon franchise, excess/under insurance and any other related matter;

(vi) estimating, measuring and determining the quantum and description ofthe subject under loss;

(vii) advising the insurer and the insured about loss minimization, loss control, security and safety measures, wherever appropriate, to avoid further losses;

(viii) commenting on the admissibility of the loss as also observance of warranty conditions under the policy contract;

(ix) surveying and assessing the loss on behalf of insurer or insured;

(x) assessing liability under the contract of insurance;

(xi) pointing out discrepancy, ifany, in the policy wordings;

(xii) satisfying queries of the insured/insurer and of persons connected thereto in respect of the claim,/loss;

(xiii) recommending applicabitity of depreciation and the percentage and quantum of depreciation;

(xiv) giving reasons for repudiation of claim, in case the claim is not covered by policy terms and conditions;

(xv) taking expert opinion, wherever required;

(xvi) commenting on salvage and its disposal wherever necessary

The appointed surveyor shall submit his report within 30 days of his appointment. In exceptional cases, the surveyor may seek extension of time up to 6 months from the insurer, under intimation to the insured. Where the report is incomplete, the insurer may seek additional report within l5 days of submission of the report by the Surveyor. Such an additional, report must be submitted within 3 weeks ofrequest having been made.

The main role of the surveyor is to assess the loss and its quantum and not to settle the claim.

Question 2

The deceased, XYZ was pursuing B.Tech. 3rd year from an Engineering Institute. XYZ had lost his life in a motor vehicle accident which occurred on 196 June,2011 at 10.40 A.M. near Haridwar. The Motor Accident Claims Tribunal (the Claims Tribunal) awarded a compensation of ₹19,50,000 to the parents of the deceased. The insurance company being Secure General Insurance Company Ltd. filed a petition claiming that the compensation awarded is exorbitant and excessive. The Claims Tribunal assumed the minimum income of the deceased as ₹25,000 per month, deducted ₹2,500 towards liability of income tax, deducted 50% towards personal and living

expenses and applied a multiplier of 14 as per the age of the deceased's mother (41 years) and computed the loss of dependency as ₹18,90,000. The Claims Tribunal further added a sum of ₹35,000 towards loss of love and affection, ₹15,000 for funeral expenses and ₹10,000 towards loss of estate. It was urged on behalf of the insurance company that the assumption of income of ₹25,000 per month was on the higher side, particularly in view of the fact that the deceased, XYZ has not been able to clear all the subjects even in the first semester and the second semester.

Based on the above, answer the following questions -

(a) Discuss the rationale behind the computation of compensation decided by the Claims Tribunal. Is the insurance company justified in its arguments ? (15 marks)

(b) Discuss the role of Motor Accident Claims Tribunal (MACT) and the powers accorded to it by the Motor Vehicles Act, 1988 in settlement of disputes and claims. (15 marks)

Answer 2(a)

In the present given case, the compensation for death ofthe deceased student is calculated on the basis of the Theory of Human Life Value. HLV can be defined as the capitalized value of the net future eamings of an individual. It is the probable income of the insured person or the total income then the person is likely to eam during the remaining part of working life. E.g. A person aged 24 will work till 60 years of age. If he is expected to eam Rs.90 lakhs throughout life, then his HLV is Rs. 90 lakhs. To calculate HLV, it is necessary to make provision for important events in one's dependents' lives. It is then necessary to calculate present household expenses, integrate the effect of inflation on expenses, and then to find out the current value of personal expenses, taking into account the current value of current liabilities and medical expenses. In the present case the HLV is computed for deceased XYZ by the Court on the same grounds.

The Claims Tribunal assumed the minimum income of the deceased as Rs. 25,000/- per month, deducted 2500/- towards liability of the income tax, deducted 50% towards personal and living expenses and applied a multiplier of 14 as per the age ofthe deceased' mother (41 years) and computed the loss of dependency as Rs. 18,90,000/-. The Claims Tribunal further added a sum of Rs. 35,000 towards loss of love and affection Rs 15000 for funeral expenses and Rs.10,000/- towards loss of estate. However the Insurance Company repudiated the claim pointing out the amount is not fair and needs to be taken on lower compensation amounts. But, the tribunal repudiated the claim of the company and has directed the compensation as per the figures arrived at by the Tribunal.

Answer 2(b)

Generally in motor accident compensation cases, especially the third party liability compensation amounts, the award is pronounced by the Motor Accident Claims Tribunal (MACT).After payment of the claim to the injured party or his legal heirs etc. The insurer can initiate action against the erring party i.e. the owner ofthe insured vehicle.

Modes of Recovery include:

— *Excess/deductible* - That portion of the claim which is to be bome by the insured is called an excess or deductible.

— Subrogation - Rights and remedies prelened against the third party.

— Contribution - This occurs when the insured property is insured by more than I insurer- in such cases recovery would be made by the lead insurer from the co insurer.

— Reinsurance - Reinsurance is the most comrnon method olrisk transfer - where the risk is re insured with reinsurers and after the claim the same is recovered from them after payment to insured.

Motor Accidents Claims Tribunal (MACT) deals with matters related to compensation of motor accidents victims or their next of kin. The tribunal deals with claims relating to loss of life/property and injury cases resulting from Motor Accidents. MACT Courts are presided over by Judicial Officers from the State Higher Judicial Service. Now these courts are under direct supervision of the Hon'ble High Court of the respective state. The Victim himself or through an advocate, in case ofpersonal injury, can approach the MACT. The application for claim can be made either by the victim, or the Legal heirs ofthe victim, or an advocate in the case of death. A minor applicant below the age of l8 years should make an application through an advocate. The claim can be made by the owner ofthe vehicle in case of property damage.

Claim arise when

(1) The insured's vehicle is damaged or any loss incurred.

(2) Any legal liability is incuned for death ofor bodily injury

(3) Or damage to the third party's property.

The claim settlement in India is done by opting for any of the following by the insurance company

(a) Replacement or reinstatement of vehicle

(b) Payment of repair charges

In case, the motor vehicle is damaged due to accident it can be repaired and brought back to working condition. Il the motor vehicle cannot be repaired, then the insured can claim for total loss or for a new vehicle. It is based on the market value of the vehicle at the time of loss. Motor insurance claims are settled in three stages. In the first stage the insured will inform the insurer about loss. The loss is registered in claim register. In the second stage, the automobile surveyor will assess the causes of loss and extent of loss. He will submit the claim report showing the cost of repairs and replacement charges etc. In the third stage, the claim is examined based on the report submitted by the surveyor and his recommendations. The insurance company may then authorize the repairs. After the vehicle is repaired, insurance company pays the charges directly to the repairer or to the insured if he had paid the repair charges. Section 110 of Motor Vehicle Act, 1939 empowers the State Govemment in establishing motor claim tribunals. These tribunals will help in settling the third party claims for the minimum amount.

Question 3

Name the persons who can make an application for compensation for an accident involving death or bodily injury to persons arising out of the use of motor vehicles ? State the relevant provisions of the Motor Vehicles Act, 1988. (5 marks)

Answer 3

The following persons can make an application for compensation for an accident involving death or bodily injury to persons arising out of use of Motor Vehicles under Section 166 of the Motor Vehicle Act, 1988 -

(a) by the person who has sustained the injury; or

(b) by the owner of the property; or

(c) where death has resulted from the accident, by all or any of the legal representatives of the deceased; or

(d) by any agent duly authorised by the person injured or all or any of the legal representatives of the deceased.

Question 4

What do you understand by condition of average' in a fire insurance contract ? How does this operate ? Explain. *(5 marks)*

Answer 4

The doctrine of average - or average clause is always applied in indemnity policies-primarily in property claims - fire and engineering. At the time of taking the policy the insured has to consider the value of the risk or subject matter of insurance-sum insured. He must ensure that the adequate value has been declared and insured. If, at the time of loss, it is found that the sum insured is less than the actual value of the subject matter, then the proportionate or ratable portion ofthe claims would be payable. The insured would therefore be his own insurer for the difference.

Insurance Contracts are strictly Contracts of indemnity. On the happening of an Insured event- Fire, the Insurer pays for the sum Insured or Market Value of the property whichever is less.

Thus if the sum insured ofa property is Rs. 30 Lacs and the Market Value ofthe same on the day of Fire was Rs.35 lacs and if the property was damaged by fire to the extent of Rs. 28 lacs, than the liability ofthe Insurance Company would be =

$$\frac{\text{Sum Insured}}{\text{Market Value}} \times \text{Loss}$$

i.e., = 3000000/3 500000*2800000

= Rs. 24 Lacs

The owner of the property would be liable for the remaining Rs. 4 lacs and would be considered to be its own Insurer for the balance.

Question 5

Why do insurers insure 'pure risks' only ? Define 'risk' and distinguish between 'pure risk' and 'speculative risk'. *(5 marks)*

Answer 5

Pure (static) risk is a situation in which there are only the possibilities of loss or no loss. The only outcome of pure risks are adverse (in a loss) or neutral (with no loss).

never beneficial.Examples of pure risks include premature death, occupational disability, catastrophic medical expenses, and damage to property due to fire, lightning, or flood.

Insurance companies generally insure only pure risks through their commercial, personal and liability insurance policies, since the law of large numbers can be applied more easily to pure risks than to speculative risks. The law of large numbers is important in insurance because it enables insurers to predict loss figures in advance.

Risk is the potential of loss (an undesirable outcome, however not necessarily so) resulting from a given action, activity and/or inaction. The notion implies that a choice having an influence on the outcome sometimes exists (or existed). Potential losses themselves may also be called "risks". Any human endeavor carries some risk, but some are much riskier than others.

Pure (static) risk is a situation in which there are only the possibilities of loss or no loss, as oppose to loss or profit with speculative risk.

Speculative (dynamic) risk is a situation in which either profit OR loss is possible. Examples of speculative risks are betting on a horse race, investing in stocks,&onds and real estate. In Business, the decision to venture into a new market, purchase new equipment's, diversify on the existing product line, expand or contract areas of operations, commit more to advertising, borrow additional capital, etc., carry risks which are inherent to the business. Speculative risk is uninsurable.

Finally, society as a whole may benefit from a speculative risk even though a loss occurs, but it is harmed if a pure risk is present and a loss occurs. Therefore, the insurers insure only pure risks.

Question 6

Explain the concept of 'treating customers fairly' with respect to policy servicing in insurance business. *(5 marks)*

Answer 6

Policy servicing is an important parameter to judge the insurance company's philosophy with respect to maintaining customer relationship in a long run. Policy servicing refers to the response given by the insurance company to any communication received from its policyholders. The Treating Customers Fairly (TCF) principle aims to raise standards in the way financial institutions cry on their business by introducing changes that will benefit consumers and increase their confidence in the financial services industry. This is a customer centric initiative aimed at improving the image and reputation of financial institutions by recognising the customers as one of the key stakeholders carefully and giving them the deserved treatment. This assumes most importance in the financial services industry keeping in mind that the customers park their hard eamed money with them and depend on them based on the expected level of servicing. Moreover, a small dissatisfaction could lead to an ineparable damage to the institutions as well. Financial Services Authority ('FSA'), UK, has introduced this as a Code for compliance by the financial institutions. Specifically, TCF aims to:

- Help Customers fully understand the features, benefits, risks and costs of the financial products they buy.

- Minimise the sale of unsuitable products by encouraging best practice before, during and after a sale.

In fact, Treating Customers Fairly is an integral part of Principle 6 of "Principles of Business" published by FSA, which states that a firm must pay due regard to the interests of the customers and treat them fairly. The retail regulatory agenda of FSA aims to achieve an effective and efficient market by treating the customers fairly. This is aimed to be achieved through a focus on capable and confident consumers, providing simple and understandable information to consumers, well managed and adequately capitalised firms which treat the customers fairly, and risk based and proportionate regulation.

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INTELLECTUAL PROPERTY RIGHTS – LAW AND PRACTICE

(Elective Paper 9.4)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Read the following case on patent law and answer the questions that follow :

Trade Related aspects of Intellectual Property Rights (TRIPS) defines geographical indication as "goods originating in the territory of a member, or a region or locality in that territory where a given quality, reputation, or other characteristic of the goods is essentially attributable to its geographical origin".

In the Indian legal system, Geographical Indication (GI) is governed by the Geographical indications of Goods (Registration and Protection) Act, 1999. A case relating to GI is that of 'Basmati rice' being patented in the United States of America (USA).

Basmati rice is regarded as the 'queen of fragrance or the perfumed one' and is also acclaimed the 'crown jewel' of South Asian rice. It is treasured for its intense fragrance and taste, famous in national as well as international markets.

This kind of rice is grown in the Himalayan hills, Punjab, Haryana and Uttar Pradesh since times immemorial. Basmati is the finest quality of rice, long grained and the costliest in the world.

Agricultural and Processed Food Products Export Development Authority (APEDA) states India to be the second largest exporter of rice after China. USA is a major importer of Basmati rice totalling 45,000 tonnes. An important case in the history of GI and bio-piracy arose in 1997.

Royal Rice Tec Inc. (RRT), a tiny American rice company with an annual income of around US $10 million and working staff totalling 120, produces a small fraction of the world's (Basmati like) rice with names 'Kasmati' and 'Texmati'. RRT had been trying to enter the world rice market since long, but in vain. On 2nd September, 1997, RRT was issued a patent for its Basmati rice lines and grains by United States Patent and Trademark Office (USPTO) bearing patent number 5663484, which gave it the ultimate rights to call the odoriferous rice 'Basmati' within US, and label it the same for export internationally. According to RRT, its invention of Basmati rice relates to novel rice lines, which affords novel means for determining cooking and which has unique starch properties, etc.

Since times immemorial, majority of farmers from India have been sustaining cultivation of Basmati rice and have been among the leading rice producers of the world. Cultivation of rice is not merely a life sustainer but also a part of socio-culture in India. Basmati rice produced in India has been exported to countries like Saudi Arabia and UK. Basmati is a 'brand name' of the rice grown in India.

Two Indian NGOs, namely, Centre for Food Safety, an international NGO that

campaign against bio-piracy, and the Research Foundation for Science, Technology and Ecology, an Indian environmental NGO, objected to the patent granted by USPTO and filed petitions in the USA. Council for Scientific and Industrial Research (CSIR), a Government of India organisation also objected to the patent granted to RRT. They demanded an amendment of US Rice Standards on the ground that the terrn 'Basmati' can be used only for the rice produced/grown in the territories of India.

According to RRT, the invention relates to novel rice lines and to plants and grains of these lines. The invention also relates to a novel means for determining the cooking and starch properties of rice grains and identifying desirable rice lines. Specifically, one aspect of the invention relates to novel rice lines whose plants are semi-dwarf in stature and give high yielding rice grains having characteristics similar or superior to those of good quality Basmati rice. Another aspect of the invention relates to novel rice lines produced from novel rice lines.The invention provides a method for breeding these novel lines. A third aspect relates to the starch index (SI) of the rice grain, which can predict the grain's cooking and starch properties and for selecting desirable segregates in rice breeding programmes.

The Government of India reacted immediately after learning of the Basmati patent issued to RRT, stating that it would approach the USPTO and urge them to re-examine the patent to a US firm to grow and sell rice under the Basmati brand name, in order to protect India's interests, particularly those of growers and exporters. Furthermore, a high level Inter-Ministerial Group comprising representatives of the Ministries and Departments of Commerce, Industry, External Affairs, Agriculture and Bio-Technology, CSIR, All India Rice Exporters Association (AIREA), APEDA and Indian Council of Agricultural Research (ICAR) was mobilised to begin an in-depth examination of the case.

In the presence of widespread uprising among farmers and exporters, India as a whole feels confident of being able to successfully challenge the Basmati patent by RRT, which got a patent for three things : growing rice plants with certain characteristics identical to Basmati, the grain produced by such plants and the method of selecting the rice plant based on a starch index (SI) test devised by RRT. The lawyers plan to challenge this patent on the basis that the abovementioned plant varieties and grains already exist and thus cannot be patented. In addition, they accessed some information from the US National Agricultural Statistics Service in its Rice Year book 1997, released in January 1998 to the effect that almost 75 per cent of US rice imports are the Jasmine rice from Thailand and most of the remainder are from India, 'varieties that cannot be grown in the US'. This piece of information is sought to be used as a weapon against RRT's Basmati patent.

Indians feel that the USPIO's decision to grant a patent for the prized Basmati rice violates the International Treaty on TRIPS. The President of the Associated Chambers of Commerce (ASSOCHAM) said that Basmati rice is traditionally grown in India and granting patent to it violates the Geographical Indications Act under the TRIPS. The TRIPS clause defines Geographical indication as "a good originating in the territory of a member, or a region or locality in that territory, where a given quality, reputation, or other characteristic of the goods is essentially attributable to its geographical origin." As a result, it is safe to say that Basmati rice is as exclusively associated with India as Champagne is with France and Scotch Whiskey with Scotland. Indians argue that just as the USA cannot label their wine as Champagne,

they should not be able to label their rice as Basmati. If the patent is not revoked in the USA, because unlike the Turmeric case, rice growers lack documentation of their traditional skills and knowledge, India may be forced to take the case to the WTO for an authoritative ruling based on violation of the TRIPS. In the wake of the problems with patents that India has experienced in recent years, it has realised the importance of enacting laws for conserving biodiversity and controlling piracy as well as intellectual property protection legislation that conform to international laws. There is a widespread belief that RRT took out a patent on Basmati only because of weak, non-existent Indian laws and the Government's philosophical attitude that natural products should not be patented. According to some Indian experts in the field of genetic wealth, India needs to formulate a long-term strategy to protect its bioresources from future bio-piracy and/or theft. British raders are also supporting India. According to Howard Jones, marketing controller of the UK's privately owned distributor Tilda Ltd.,"true Basmati can only be grown in India. We will support them in any way if it's necessary". The Middle East is also according support by labeling only the Indian rice as Basmati. Government and government agencies have gathered the necessary data and information to support their case and to prevent their cultural heritage being taken away from them.

Questions -

(a) *Whether Royal Rice Tec Inc. is guilty of bio-piracy ? Explain.* *(10 marks)*

(b) *Discuss whether the decision of the USPTO of granting patent for the valued Basmati rice violates TRIPS.* *(10 marks)*

(c) *How does the patent granted to RRT by USPTO impact the farmers in India ?* *(10 marks)*

(d) *Whether adequate legislations exist in India with respect to geographical indications ? Discuss the salient features.* *(10 marks)*

(e) *Explain the provisions for registration of geographical indications in India.* *(10 marks)*

Answer 1(a)

Bio-piracy in general can be defined as the practice of commercially exploiting naturally occurring biochemical or generic material, especially by obtaining patents that restrict its future use, while failing to pay fair compensation to the community from which it originates. It is a manipulation of the Intellectual Property Rights by the corporations, entities and persons to gain an exclusive control over the national genetic resources, without giving adequate recognition and remuneration to the original possessors of those resources. Indigenous people possess important traditional knowledge that have allowed them to sustainably live and make use of biological and genetic diversity within their natural environment for generations. Traditional knowledge naturally includes a deep understanding of ecological processes and the ability to sustainably extract useful products from the local habitat. Example of bio-piracy includes the recent patents granted by the US Patent and Trademark Office to different American companies on ‘Turmeric’, ‘Neem’ and most notably, ‘Basmati Rice’. All three products are indigenous to the Indian subcontinent since time immemorial.

RRT's actions constitute bio-piracy because it violated the provisions of the Convention on Biological Diversity ('CBD' in short), which provides for State's sovereignty over its genetic resources. The CBD aims to bring about a system for the conservation and sustainable use of biological diversity and the fair and equitable sharing of benefits arising from the use of their genetic resources. The manner in which RRT established its patent demonstrates that it has ignored the contributions of the local communities in the production of Basmati and that it does not intend to share the benefits accruing from the use of the genetic resources. This includes both the informal contributions of the farmers who have been growing Basmati for hundreds of year in India and the neighbouring sub-continents, as well as the more formal, scientific breeding work that has been done by rich research institutes to evolve better varieties of Basmati. RRT has capitalized on this work of the indigenous community by taking out a Patent on Basmati and intends to monopolize the commercial use of a past research, without giving any recognition or remuneration to those who played a key role in the evolution and breeding of Basmati rice in its natural habitat.

Theft involved in the Basmati patent is therefore classified threefold namely a theft of collective intellectual and biodiversity heritage on Indian farmers, a theft from Indian traders and exporters whose markets are being stolen by RRT, and finally a deception of consumers since RRT is using a stolen name Basmati for rice which are derived from Indian rice but not grown in India, and hence are not the same quality.

RRT has unfairly appropriated and exploited the genetic resources in this case by attempting to gain an exclusive control on its development and propagation through a legal process that threatens the traditional rights of the original possessors of the resource. The key concern relates to RRT's use of the term 'Basmati' to describe its rice lines and grains. 'Basmati' is associated with the specific aromatic rice variety grown in India and by taking out a Patent on the use of the term to describe its invention, RRT has potentially reversed the culpability, and made India the violator of RRT's legally protected rights despite the fact that the latter are the original possessors and breeders of the 'Basmati' rice. RRT is guilty of bio-piracy.

Answer 1(b)

The grant of a Patent to RRT on Basmati does contravenes certain provisions of TRIPS. The TRIPS Agreement provides for certain standards to be fulfilled before grant of a protection in the form of Intellectual Property Rights which are particularly relevant for the purposes of determining whether there was any act of bio-piracy involved in the present case.

RRT's patent on Basmati violates Article 22 of the TRIPS, which deals with Geographical Indications. As defined under Article 22(1) of TRIPS, Geographical Indications are indications which identify a good as originating in the territory of a member, or a region or locality in that territory, where a given quality, reputation or other characteristic of the good is essentially attributable to its geographical origin.

For instance, wines and liquors are most commonly associated with Geographical Indications of their place of origin. The term "Champagne" can only be used to describe a wine that has been produced in the Champagne region of France, the area from which the wine derives its name. Wine with similar characteristics but produced in another part of the world, cannot be described a "Champagne".

"Champagne" remains an exclusive product and the name as the exclusive property of the French company producers. A similar case of Geographical Indication is that of a "Scotch", a whisky, which is produced in the Scottish highlands. This protection for Geographical Indications for wines and liquors is outlined in Article 23 of the TRIPS.

Basmati falls in this category because it enjoys the same closely linked and exclusive relationship with its place of origin in India. In India, Basmati is grown mainly in some scattered districts of Punjab, Haryana and Uttar Pradesh. India grows tons of rice annually. Thus, it is clear that Basmati rice, as it is traditionally recognized, is geographically unique in its origin.

The Basmati Patent resulted in a brief diplomatic crisis between India and United States with India threatening to take the matter to WTO as a violation of TRIPs, because a GI product cannot be patented under the provision of TRIPs. However, ultimately, due to review decisions by the United States Patent Office, RRT has lost most of their claims of the patent, including, most importantly, the right to call their rice "basmati."

There is a precedent also for the recognition of Basmati as a Geographical Indication by the International Buyers. The European Commission recognizes India's and other neighbouring sub-continent's rights over products bearing their distinctive geographical indications, allowing only Basmati rice that has been grown in India and neighbouring sub-continent to be labelled as such.

Similarly, the code of practice for rice in the UK, the largest market for Basmati rice in Europe, describes long grain, aromatic rice grown only in India and neighbouring sub-continent as Basmati.

Answer 1(c)

RRT's patent could impact Indian farmers in the following two possible ways:

(i) By displacement of Basmati exports from India; and

(ii) By monopolizing the Basmati seed supplies.

Regarding the first possible inroads which may be made by the USA into the South Asian export markets, it is a matter of concern to the Indian farmers. In 1995, USA produced 7.89 million metric tons of rice and in the same year India produced 122.37 million metric tons of rice.

American rice exports are significantly greater than India, implying that USA has a greater production surplus. In 1994 itself, USA exported more volumes of rice as compared to India and its neighbouring sub-continent. Therefore, owing to the RRT's patent, it seems that potential exists for USA to displace Indian Basmati exports.

Criticism from Indian rice farmers logically ensued, as many were forced to pay royalties to the conglomerate. The production and cultivation of Basmati has with it a history dating back to centuries ago. For farmers, the grain is an entity that is constantly evolving. In the context of India, Basmati rice has always been considered a common resource dependent upon word of mouth knowledge and transfer. Using this logic, RiceTec alleged that the 'Basmati' name was in public domain, and that by patenting it; they were in actuality protecting its name and origins. RRT soon came out with hybrid versions: Kasmati, Texmati, Jasmati, which for rural farmers clearly illustrated the profit based

interest of the conglomerate. Through its acquisition, RRT patented some 22 varieties of the rice. One of which being Basmati 867, a rice grain which was very similar to original Basmati but was advertised to have a less chalky more refined taste. The severity of RRT's bio piracy cannot be underestimated, as the conglomerate was claiming to have invented the physical characteristics of Basmati such as the plant height and grain length. By claiming ownership of the rice plant itself, RRT was directly threatening rural farming communities.

A second and more serious threat is that, through its patent, RRT could acquire a monopoly over Basmati seed supply to the sub-continent. It is a premier developer of commercial hybrid rice varieties in the USA. A precedent exists that foreign agri-business companies have bought hybrid seeds to Third World Countries. For example, Monsanto has recently undertaken a joint venture with Grameen Bank in Bangladesh to distribute its hybrid seeds through loan packages to small farmers.

Hybridization is likely to harm small farmers more as they are less able to absorb the higher seed costs. In its extreme form, such hybridization could harm genetic diversity and deplete farmlands of their intrinsic resources.

Answer 1(d)

In India, the legal system for Geographical Indication ('GI' in short) protection has been developed very recently. The provisions in that regard are contained in The Geographical Indications of Goods (Registration and Protection) Act ('GI Act' in short) which was enacted in the year 1999 and came into force only in September 2003.

Salient Features of Legal Protection to Geographical Indications in India:

1. *Comprehensive Definition of GI* : From the perspective of a developing country, one of the best features of the GI Act is the comprehensive definition of GI laid down therein, whereby agricultural, natural and manufactured goods all come under the ambit of the term GI.

2. *Detailed Registration Mechanism* : The Act provides a mechanism for registration of GIs, establishes a GI Registry, and elaborates the concept of 'authorized user' and 'registered proprietor'. Section 11of the Act provides that any association of persons, producers, organization or authority established by or under the law can apply for registration of a GI.

3. *Extended Protection* : Another important aspect of the Act is the possibility of protecting a GI indefinitely by renewing the registration when it expires after a period of ten years.

4. *Higher Level of Protection to Notified Goods* : The Act provides a higher level of protection for notified goods and the corresponding remedies for their infringement. In the Indian context, the GI Act has tried to extend the additional protection reserved for wines and spirits mandated by TRIPS to include goods of national interest on a case to case basis. Section 22(2) of the Act endows the Central Government with the authority to give additional protection to certain goods or classes of goods.

5. *Restrictions on Appropriation, Assignment and Transmission* : Section 25 of the Act, by prohibiting the registration of a GI as a trademark, tries to prevent appropriation of a public property in the nature of a GI by an individual as a trademark, leading to confusion in the market. Also, according to section 24 of the Act, a GI cannot be assigned or transmitted. The Act recognizes that a GI is a public property belonging to the producers of the goods concerned; as such, it cannot be the subject matter of assignment, transmission, licensing, pledge, mortgage or any contract for transferring the ownership or possession.

6. *Infringement of Geographical Indications* : The remedies relating to the infringement of Geographical Indications are similar to the remedies relating to the infringement of Trademark. Similarly, under the (Indian) Geographical Indications of Goods (Registration and Protection) Act, 1999, falsification of a Geographical Indication will carry a penalty with imprisonment for a term which may not be less than six months but may extend to three years and with fine which may not be less than INR 50,000 but may extend to INR 2,00,000. Action for infringement of a Geographical Indication may be instituted at a District Court or High Court having jurisdiction.

Available relief include: -

- Injunction.
- Discovery of documents.
- Damages or accounts of profits.
- Delivery-up of the infringing labels and indications for destruction or erasure.

Answer 1(e)

Provisions for the registration on Geographical Indication are as follows:

Section 8 of the of Geographical Indications of Goods (Registration & Protection) Act, 1999 provides that a geographical indication may be registered in respect of any or all of the goods, comprised in such class of goods as may be classified by the Registrar and in respect of a definite territory of a country, or a region or locality in that territory, as the case may be.

The Registrar may also classify the goods under in accordance with the International classification of goods for the purposes of registration of geographical indications and publish in the prescribed manner in an alphabetical index of classification of goods.

Any question arising as to the class within which any goods fall or the definite area in respect of which the geographical indication is to be registered or where any goods are not specified in the alphabetical index of goods published shall be determined by the Registrar whose decision in the matter shall be final.

Application : According to Section 11 of the Act, an application for registration must be made before the Registrar of Geographical Indications by an association of persons or producers or an organization or authority established by or under any law for the time being in force representing the interest of the producers of the concerned goods.

Particulars of Application : The application must be made in an appropriate form giving details with respect to the nature, quality, reputation or other characteristics which are due exclusively or essentially to the geographical environment, manufacturing process, natural and human factors, map of territory of production, appearance of geographical indication (figurative or words), list of producers, along with prescribed fees.

Examination of Application : The examiner will make a preliminary scrutiny for deficiencies and in case of deficiencies the applicant shall have to remedy it within a period of one month from the date of communication of such deficiencies.

Acceptance or Refusal of Application : The Registrar may accept, partially accept or refuse the application. In case of refusal, the Registrar will give written grounds for non-acceptance. The applicant must within two months file its reply. In case of re-refusal, the applicant can make an appeal within one month of such decision.

Advertisement of the Application : Section 13 of the Act states that the Registrar shall, within three months of acceptance of the application for registration of a GI, but before its registration, may advertise the application in the GI Journal.

Registration : As per section 16 of the Act, if there is no opposition to the grant of GI, the Registrar will grant a certificate of registration to the applicant and its authorized users.

Question 2

Read the following case and answer the questions given at the end :

The plaintiff, Polymer India Ltd., is a leading manufacturer and distributor of quality products made using plastic moulding technology. Its products include toys, school furniture and playground equipment. The plaintiff is also the registered proprietor of the trademark 'PLAY' since 25th August, 2005.

The plaintiff sued eight defendants namely Playwell Impex Pvt. Ltd., Mayank, Ms. Meenakshi, Pawan, Vishal, Darshan, R.P. Associates and Funko India who are involved in manufacture and distribution of similar products. The plaintiff claimed relief of permanent injunction to restrain the defendants from infringing its copyright, common law rights in designs and passing off of deceptively similar products.

An ex parte ad interim injunction was granted to the plaintiff by a Court vide its order dated 7th August, 2015 and the goods of the defendants were seized by the Court Commissioner appointed vide the same order.

The plaintiffs contentions are :

— *That the products of plaintiff are unique and conceptualised individually, which involves study of the market, preparation of the drawings, drawing a feasibility report, preparation of a new colour scheme, finalisation of dimensions, etc.*

— *That the defendant Playwell Impex Private Ltd. is engaged in the business of manufacture, distribution and sale of toys in collusion with the other defendants including R.P. Associates who was earlier the distributor of plaintiffs products and Darshan, who is an ex-employee of the plaintiff. The defendant Playwell Impex Pvt. Ltd. has launched a range of toys which are identical and deceptively*

similar to the toys made by the plaintiff and is thereby passing off its goods as those of the plaintiff, infringing the bundle of intellectual property rights of the plaintiff in its products.

— *That the toys manufactured and sold by the defendants under the brand FUNKO are a substantial re-production and colourable imitation of the products of the plaintiff.*

— *That there is a clear distinction between an original artistic work and a design derived from it for industrial application on a product. The original artistic work which may be used to industrially produce the designed article would fall within the meaning of artistic work defined under section 2(c) of the Copyright Act, 1957 and would be entitled to copyright protection as defined under section 2(d) of the Designs Act, 2000.*

— *That the defendants in their written statement have admitted the e-mail of the defendant Darshan to the defendant Playwell Impex Pvl Ltd. forwarding the brochure of the toys of the plaintiff and therefrom it is evident that the defendant Playwell Impex Pvt. Ltd. is replicating from the brochure of the plaintiff.*

The defendants' contentions are :

— *That the drawing in which the plaintiff claims a copyright does not constitute a design within the meaning of section 2(d) of the Designs Act, 2000 and is thus, not capable of being registered under the Act.*

— *That the plaintiff has no right to claim protection of design without any registration.*

— *That the plaintiffs toys which are being manufactured since the year 1992, are not novel and similar products are available in the market for ages.*

— *That the plaintiffs products to which the design has been applied have been reproduced by it, more than 50 times by an industrial process.*

— *That the interim injunction granted is not justified when infringement is not proved.*

Questions -

(a) Discuss the relation between the Copyright Act, 1957 and the Designs Act, 2000. (5 marks)

(b) What will be your decision on the interim injunction ? Will you confirm or vacate the same ? Give reasons. (5 marks)

(c) Is the plaintiff entitled to copyright protection ? Can artistic works related to design be protected under the Copyright Act, 1957 ? (10 marks)

(d) Explain the copyright protection to foreign works in India. What are the conditions for such copyright protection in India ? (10 marks)

Answer 2(a)

Section 2 (d) of the Design Act, 2000 defines the term 'Design' and expressly excludes "any artistic work as defined in clause (c) of section 2 of the Copyright Act, 1957" from its scope.

Section 2 (c) of the Copyright Act defines an "Artistic Work" to include any work of artistic workmanship.

Therefore, an artistic work does not fall within the definition of a Design under the Design Act, 2000. Section 15 of the Copyright Act declares that a copyright does not subsist under the Act in any design which is registered under the Design Act. Furthermore, the said section declares that *"Copyright in any design, which is capable of being registered under the Design Act, 2000, but which has not been so registered, shall cease as soon as any article to which the design has been applied has been reproduced more than 50 times by an industrial process by the owner of the copyright, or, with his licence, by any other person."*

Reading together the aforesaid provisions in the Copyright Act and the Design Act, it may be concluded that an artistic work will not fall within the definition of a Design under the Design Act, 2000, but if it is related to a Design, then they can be protected under the Design Act and not under the Copyright Act.

Answer 2(b)

In the present case, analysing the relationship and the interplay between the Copyright Act and the Design Act, the artistic works which are related to a Design can be protected under the Designs Act and not under the Copyright Act. The previous ex parte injunction granted to the plaintiff deserves to be vacated in favour of the defendants. The application of the Plaintiff for the interim relief is dismissed. Further, the applications made by the defendant for vacation of the ex parte order and return of its goods are allowed. The goods seized by the Court Commissioner/s shall be forthwith released to the defendants.

Answer 2(c)

Considering the inter-relationship between the Copyright Act, 1957 and the Design Act, 2000, it is appropriate to state that if a design is applied to an article and re-produced for more than 50 times by an industrial process after making a drawing, then the drawing cannot be treated disjunctively from the said design and the copyright cannot be vested in such a drawing. Section 15 (2) of the Copyright Act expressly provides for the end of the said protection.

The Design and Copyright law are interrelated by Section 15(2) of the Copyright Act, 1957 and Section 2(d) of The Design Act, 2000. Section 15(1) of the Copyright Act categorically prohibits copyright protection if a design is registered under the Design Act. Further, sub-section 2 of Section 15 states that, if a design is capable of being registered under the Design Act but the same has not been registered, such design will cease to have copyright protection as soon as an article to which such design is applied is reproduced more than 50 times by an industrial process. Section 2(d) of The Design Act excludes any artistic work as defined in Section 2(c) of the Copyright Act from the definition of 'design' under the Design Act.

The plaintiff's products manufactured more than 50 times by an industrial process and their design are registrable under the Design Act. No protection on the basis of copyright can be given to Plaintiff.

Answer 2(d)

As per section 40 of the Copyright Act, 1957, the Central Government may, by order published in the Official Gazette, direct that all or any provisions of the Act shall apply in respect of the work of any foreign country.

Indian Copyright law is presently at parity with the international standards as contained in TRIPS. The Copyright Act, 1957 after the amendment made in the year 1999 fully reflects the Berne Convention on Copyrights and the Universal Copyrights Convention, to which India is a party. India is also a party to the Geneva Convention for the Protection of Rights of Producers of Phonograms and is an active member of the World Intellectual Property Organization (WIPO) and UNESCO. The works of such foreign country are thus protected in India under section 40 of the Copyright Act 1957, read in conjunction with the International Copyright Order 1999.

Under the Copyright Act, 1957 works of foreign authors/owners are accorded the same protection in India to which the Indian citizens are entitled to under the Act.

Conditions for the Copyright Protection of Foreign Work

The Copyright Protection to a foreign work is subject to certain conditions which are mentioned below:

(i) That before making an order under this section in respect of any foreign country (other than a country with which India has entered into a treaty or which is a party to a convention relating to copyright to which India is also a party), the Central Government shall be satisfied that that foreign country has made, or has undertaken to make, such provisions if any, as it appears to the Central Government expedient to require for the protection in that country of works entitled to copyright under the provisions of this Act;

(ii) That the order may provide that the provisions of this Act shall apply either generally or in relation to such classes of works or such classes of cases as may be specified in the order;

(iii) That the order may provide that the term of copyright in India shall not exceed that which is conferred by the law of the country to which the order relates;

(iv) That the order may provide that the enjoyment of the rights conferred by this Act shall be subject to the accomplishment of such conditions and formalities, if any, as may be prescribed by the order;

(v) That in applying the provisions of this Act as to ownership of copyright, the order may make such exceptions and modifications as appear necessary, having regard to the law of the foreign country;

(vi) That the order may provide that this Act or any part thereof shall not apply to works made before the commencement of the order or that this Act or any part thereof small not apply to works first published before the commencement of the order.

Question 3

Explain the grounds for refusal of registration of a trademark. *(5 marks)*

Answer 3

A trademark is required to be either inherently distinctive or capable of distinguishing its goods by acquiring distinctiveness if used for some period of time. The Trademarks

Act, 1999 provides for absolute and relative grounds for refusal of registration of a trademark.

Absolute Grounds – (Section 9 of the Act)

The First Rule – [sub-section (1)]

- The mark lacks distinctiveness;
- The mark is descriptive of the characteristics of the goods or services;
- The mark consists exclusively of marks or indications which have become customary or in the bonafide and established practices of the trade.

Exception to the above Rule – the Proviso to sub–section (1)

Before the date of application for registration, if the mark has acquired a distinctive character as a result of the use made of it or if the mark is a well–known mark, the mark shall not be refused registration.

Second Rule – [sub– section (2)]

- The mark is of such nature as to deceive the public or cause confusion;
- The mark is likely to hurt religious sentiments;
- The mark comprises scandalous or obscene matter;
- The use of the mark is prohibited under the Emblems and Names (Prevention of Improper Use) Act, 1950;

The Third Rule – [sub-section (3)]

If the mark consists exclusively of the shape of the goods (i) resulting from nature of the goods; or (ii) which is necessary to obtain a technical result; or (iii) which gives substantial value to the goods.

Relative Grounds (Section 11 of the Act):

The First Rule – [sub– section (1)]

The mark is identical or similar to an earlier trademark and the goods are identical or similar to the goods of the earlier trademark.

The Second Rule – [sub– section (2)]

The mark is identical or similar to an earlier trademark and use of such a mark would allow the applicant to gain an unfair advantage of or damage the reputation of the earlier trademark though goods may not be similar.

Note : For the First and Second Rule, "Earlier Trademark" means a "registered mark" or a "well known mark".

The Third Rule – [sub– section (3)]

The use of the mark in India should be prevented by virtue of any law, in particular, the law of passing off protecting an unregistered trademark or by virtue of the law of copyright.

'Honesty' is an Exception – [sub-section (4) of section 11 read with section 12]

Section 12 of the Trademarks Act, 1999 permits registration of "honest concurrent users". For availing the benefit thereof, the applicant must be a *bonafide* prior or concurrent user of the mark.

Question 4

What is a trade secret ? How are trade secrets protected ? *(5 marks)*

Answer 4

A trade secret is any kind of information that is secret and not generally known in the relevant industry giving the owner an advantage over competitors. In other words, any information which can be used in business and is sufficiently valuable to afford an actual or potential economic advantage over others is a trade secret. Trade secret includes formulas, patterns, methods, programs, techniques, processes or compilations of the information providing competitive edge.

Trade secrets are not protected by any law as a registered trademarks or a patent. Article 39 of TRIPS agreement protects for trade secrets in the form of 'undisclosed information' and provides a uniform mechanism for the international protection of trade secrets. These are protected by a variety of civil and commercial means. Any other person (including employees) with the potential to come to know the secret is asked to sign a confidentiality and/or non-disclosure agreement. Violation of these agreements generally entails financial penalties.

In India, the only remedies available for the protection of trade secrets are civil or equitable remedies for a breach of confidence cause of action. They include:

- an award of injunction "preventing the third party from disclosing the trade secrets," and "confidential and proprietary information," and;
- In the case of "for any losses suffered due to disclosure of trade secrets." The court may order any damages or compensation to be given to the plaintiff. The court may also order the party at fault to "deliver up" such materials.

Question 5

Explain the restrictive trade practice of tie-in arrangements in IPR licensing. *(5 marks)*

Answer 5

Tie-in-Arrangement in an intellectual property licencing arrangement requires the licensee to obtain raw materials, spare parts, and intermediate products for use with licensed technology only from the licensor or its nominees. Such arrangements also oblige the licensee to use the personnel designated by the licensor. The purpose is to preserve exclusive right to supply necessary processed or semi-processed inputs, to maintain quality control and to expand the licensor's profit margin.

The tie-in clauses in an agreement generally result in a monopoly control of the supply of equipment and other inputs for the supplying enterprises, leading to 'transfer pricing', 'transfer accounting' or uneconomic output'. Due to tie-in clauses, licensor

charges higher price for inputs and equipment. The use of tie-in clauses not only affects production costs through the overpricing of inputs but may have important indirect effect on the import substitution, export diversification and growth efforts of the licensee.

Tie-in-arrangements fall foul of the provisions relating to anti-competitive practices under the Competition Act, 2002.

Question 6

Explain the usage of 'excess profits method' for valuation of intangibles. (5 marks)

Answer 6

'Excess Profits Method' in reference to intangibles looks at the currents value of the net tangible assets employed as benchmark for an estimated rate of return. This is used to calculate the profits that are required in order to induce investors to invest into those net tangible assets. Any return over and above those profits required in order to induce investment is considered to be the excess return attributable to Intellectual Property. While theoretically relying upon future economic benefits from the use of the asset, the method has difficulty in alternative usage of assets. But worldwide, future economic benefits are used to arrive at current valuation of intangible assets.

The excess operating profits method determines the value of the intellectual property by capitalising the additional profits generated by the business owning the property over and above those generated by similar businesses, which do not have the benefit of the property. There are various ways in which the excess profits may be calculated, for example by reference to a margin differential or comparing the return on capital employed earned by the business owning the property with that earned by companies without such benefit. The calculated excess operating profits expected to be earned over the life of the asset in question are then discounted to the present day to arrive at a value for the asset.

It is important, if using this method, to ensure that the excess profits identified are specifically attributable to the intangible asset in question and not to some other factor such as an efficient production facility or distribution network that relates to the business as a whole.

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INTERNATIONAL BUSINESS LAWS AND PRACTICES
(Elective Paper 9.5)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Read the following and answer the questions given at the end :

Indian Iron and Steel Industry - Requires cautious strategic planning Iron and steel sector is the sheet-anchor of a country's overall industrial growth as it provides an indispensable basic input for various industries. This industry commands large backward and forward linkages that pave the way for further industrialization. For these and many other reasons, steel industry is often considered as the backbone of an economy.

The Global Steel Industry

Increasing modernisation in the twenty-first century has led to the doubling of global steel production. Asia and the Middle East remained the most vibrant regions in terms of production with more than 7.0% CAGR. Further, regions like EU, Africa and North America exhibiled contraction, registering negative CAGR of around 1.2%. At the country level, China remained by far, the largest producer of crude steel accounting for nearly half of the world's steel production. Among the top 10 exporters of iron and steel in the world, China is leading with highest share and India ranked 11th in the list of exporters. The world market for steel amounted to US $1.3 trillion in 2015, with production levels of 1,694.73 million tonnes and consumption at 1,545.50 million tonnes.

The reality is that steel supply has outpaced demand over the last five years. The industry is facing a very challenging situation because of the structural over supply of steel in international markets. The global composite carbon steel prices plunged down, owing to a demand-supply mismatch. This was the ninth consecutive decline in global steel prices during May,2014 to February, 2015. The dumping of steel has caused a huge pressure on the net sales realisations and the margins of global steel companies.

The collapse in the price of steel is mainly the result of falling demand and, until recently, rising production in China. Between the year 2000 and 2014, global steel production doubled from around 800 million tonnes to around 1.6 billion tonnes a year, mainly driven by rising output in China. Until the year 2014, Chinese demand rose at approximately the same rate as its steel mills could produce, meaning that the impact on the rest of the world was limited. But as its construction boom came to an end, demand sagged; prompting the country's state owned steel makers to sell their growing surpluses in foreign markets.

Further, the recent devaluation of Chinese Yuan in October, 2015 has improved prospects of higher steel exports from China. With a huge exportable surplus, China is not just a growing threat for India, but to almost all the steel making nations in the world.

Britain's steel industry is not the only one in the West feeling the pinch from low steel prices. Both Belgium and Italy are spending public money to keep their steel mills running and the American industry is facing job losses.

Globally, there is structural over capacity in steel sector, which has led these steel producing countries to export steel products. Contradicting to global steel demand, India is one of the countries, where steel demand has grown in the first nine months of the year 2015. This has given an opportunity for the international steel players to make India an export dumping ground.

The Indian Steel Industry

India's economic growth is contingent upon the growth of its steel industry. Consumption of steel is taken to be an indicator of economic development. While steel continues to have a stronghold in traditional sectors such as construction, housing and transportation, special steels are increasingly used in engineering industries such as power generation, petrochemicals, auto industry and fertilizers. India occupies a central position on the global steel map, with the establishment of new state-of-the-art steel mills, acquisition of global scale capacities by players, continuous modernisation and upgradation of older plants, improving energy efficiency and backward integration into global raw material sources. The Indian steel sector was the first core sector to be given complete freedom from the licensing regime. There are at present eleven integrated steel plants and eighteen secondary mini-steel plants in the country.

The steel industry in India has also witnessed a rapid rise in production over the past few years at the backdrop of enhancement of capacity. This has resulted in India becoming the third largest producer of crude steel ahead of UK and Brazil, and just behind China and Japan and the largest producer of sponge iron in the world.

Steel accounts for about 2 per cent of India's GDP and holds a 6 per cent share in the industrial production of the country. With construction and infrastructure sectors together occupying a significant share in total steel demand in India, the revival of these two sectors is expected to cause a positive effect on the domestic steel industry. On account of steady gtowth in the domestic steel consumption, India became the third largest consumer (China being first) of steel globally in 2009, and continues to remain so till today.

At the aggregate level, the markets of North America, Asia and Oceania are regions where Indian iron and steel products are competitive and these regions have also exhibited strong import demand for the products. In Europe and Africa, Indian steel products are competitive, but the growth in import demand has been frail.

In terms of value, India's exports of iron and steel in the year 2008-09 was less than its imports, leading to a trade deficit of US $0.6 billion. However, after having witnessed a trade deficit for a number of years, it 2013-14 India displayed a trade surplus. But in 2015, a marginal trade deficit was experienced. Import continued to hurt the industry, rising 29 per cent to 8.4 million tonnes, while exports decreased by 30 per cent to 2.9 million tonnes till the end of December, 2015 (becoming net importers).

Besides all this positivism, the Indian steel industry is also not free from global crisis. The industry is struggling for last few years to sustain itself and trying too hard to contribute in the national economic growth.

Major drawbacks of Indian Steel Industry

Following are some common drawbacks faced by the Indian iron and steel industry:

— *The industry requires large capital investment which a developing country like ours cannot afford. Many of the public sector integrated steel plants have been established with the help of foreign aid.*

— *During the last two decades after the oil crisis, steep hike in energy costs and escalation of costs of other inputs reduced the margin of profit of the steel plants. This resulted in lower levels of investment in technological developments.*

— *Material value productivity in India is still very low. In Japan and Korea, less than 1.1 tonnes (and in several developed countries 1.05 tonnes) of crude steel is required to produce a tonne of saleable steel. In India, the average is still high at 1.2 tonnes.*

— *The per capita labour productivity in India is at 90-100 tonnes per year which is one of the lowest in the world. The labour productivity in Japan, Korea and some other major steel producing countries is about 600-700 tonnes per man per year. At Gallatin steel, a mini mill in the U.S., there are less than 300 workers to produce 1.2 million tonnes of hot rolled coils. A comparable firm in India employs 5,000 workers.*

— *Raw material scarcity is on the top of the agenda. India is very much dependent on imported coking coal. Approximately 60-65 per cent of the domestic coking coal requirements are met through imports due to unavailability of appropriate quantities in the country.*

Industry's Expectation

The Indian steel industry is demanding protection from the crisis. The industry wants longer duration duties like anti-dumping duties to counter cheaper imports. Domestic steel makers have urged the government to keep steel out of the purview of any future free-trade agreements (FIAs) and also review the existing pacts to ensure that their interests are safeguarded. Taking advantage of duty benefits under FTAs, steel makers from Japan and Korea have already become a serious threat to Indian steel industry.

Government Measures

The Government of India has taken this matter seriously by implementing following steps not only to protect but also to develop the industry :

— *It imposed a 20 per cent ad valorem safeguard import duty on some steel products.*

— *It has also set a floor price or minimum import price (MIP) on 173 steel products to deter countries led by China from undercutting local mills, the first such move in more than 15 yean. Due to this, imports became costlier by 26-70 per cent helping the local steel players to compete better.*

— *Further it imposed anti-dumping duty on stainless steel imports, as it tries to protect the struggling domestic industry from cheap imports. Some other countries have also adopted the same practices; countries like America and Australia have imposed dumping duties on Chinese steel. Indian steel makers may also attract anti-dumping duty in Canada.*

— *Out of nearly two dozen sectors identified by the government as focus areas under the 'Make in India campaign, the cost of steel is crucial to the competitiveness of manufacturing in at least nine industries - automobiles, automobile components, construction, defence manufacturing, electrical machinery railways, renewables, thermal power, and oil and gas.*

— *Additionally, the government's focus on rural-urban (rurban) cluster development is also likely to push-up demand for steel. The budget outlay of 72,21,246 crore on infrastructure including railways meets the long standing demand from core sectoral industries such as cement and steel.*

— *For ensuring quality of steel, several items have been brought under a quality control order issued by the Government.*

Global challenges ahead

The Indian steel industry is expected to face following global challenges till 2025 and beyond :

— *Australia and Brazil are expected to supply about 90 per cent of all seabome iron ore by 2022. This increase in supply and moderation in demand may continue to exert pressure on iron ore prices.*

— *China, which is currently a net importer of scrap, is expected to have a surplus of scrap by 2025. This will decrease demand and push down the prices of other raw materials such as coking coal and iron ore.*

— *Shale gas, emerging as cheap source of fuel, could change the competitive landscape in steel making. Countries such as Iran, Saudi Arabia and Mexico are using natural gas and iron ore to make direct reduced iron (DRI). This process does not need coking coal.*

— *Ongoing research in the steel industry, especially to meet the environmental standards, will bring in a lot of technological changes in coming years which are quite expensive.*

Suggested Remedies

— *India needs public and private investment in urban and rural infrastructure, real estate, roads, railways, civil aviation and irrigation to boost-up steel consumption.*

— *Given the fact that steel market across the globe is vulnerable to global conditions, India needs to be more proactive in diversifying its export markets. It could, therefore, adopt a similar strategy as Brazil, focusing on geographically nearer markets where it has freight advantage, such as Nepal, Bangladesh and Sri Lanka.*

— *Indian companies should target export destinations for steel sheet products, such as the Middle East and Africa, where they have a freight advantage over China, Japan and South Korea.*

Questions -

(a) Explain the consequences in the global steel industry due to demand scarcity. What are the causes, according to you, that lead the industry to crisis ?
(10 marks)

(b) Prove why steel industry is considered as the backbone of Indian economy ?

What are the common problems that the industry is facing in its regular operations? Being an international expert, suggest steps to boost the industry. (10 marks)

(c) What do you mean by FTA ? What are its merits and demerits ? Explain how the Indian steel makers are in threat from Japan and Korea due to FTA. (10 marks)

(d) "The domestic steel players need to be protected. " Discuss the steps implemented by the government so far as to protect the industry. (10 marks)

(e) Differentiate between 'dumping' and 'anti-dumping'. Why do you think that the imposition of anti-dumping duty on steel imported by India is beneficial for the Indian industry ? Explain the challenges the Indian steel industry is anticipating from global players in coming years. (10 marks)

Answer 1(a)

The industry is facing a very challenging situation because of the structural oversupply of steel in international markets, resulting in almost all the countries looking to export steel products. The global composite carbon steel prices plugged-down, owing a demand-supply mismatch. The dumping of steel has caused a huge pressure on the net sales realizations and the margins of global steel companies. Britain's steel industry is not the only one in the West feeling the pinch from low steel prices. Both Belgium and Italy are spending public money to keep their steel mills running and the American industry is facing of job losses.

The collapse in the price of steel is mainly the result of falling demand and, until recently, rising production in China. Between 2000 and 2014, global production doubled from around 800 million tonnes to around 1.6 billion tonnes a year, mainly driven by rising output in China. Until 2014, Chinese demand rose at approximately the same rate as its steel mills could produce, meaning that the impact on the rest of the world was limited. But as its construction boom came to an end, demand sagged, prompting the country's state-owned steelmakers to sell their growing surpluses on foreign markets.

Answer 1(b)

Iron and steel industry is one of the most important basic or 'classical' industries of India providing base for overall industrialization of country. Its role in the economic development, inter-alia in industrial development of the country cannot be under-estimated. Its importance for national defence is equally great, since armaments of every kind from the smallest pistol to the biggest armada are made of iron and steel. Economists and policy makers, world-over, regard per-capita use of steel as index of its industrial progress of any country. It is natural, therefore, that any country which aspires for industrial development should build up its steel industry. The steel account for about 2 per cent of India's GDP and holds a 6 per cent share in the industrial production of the country. With construction and infrastructure sectors together occupying a significant share in total steel demand in India, the revival of these two sectors are expected to cause a positive effect on the domestic steel industry. On account of the steady growth in the domestic steel consumption, India became the third largest consumer (China being first) of steel globally in 2009, and continued to remain so till today.

In terms of value, India's exports of iron and steel in the year 2008-09 was less than its imports, leading to a trade deficit of US$0.6 billion. However, after having witnessed

a trade deficit over a number of years, in 2013-14 India displayed a trade surplus. But in 2014-15 a marginal trade deficit was experienced. Imports from low cost suppliers continued to hurt the industry thus rising 29 per cent to 8.4 million tonnes, while exports decreased to 30 per cent to 2.9 million tonnes till the end of December 2015 thus making India a "net importer" of steel once again.

Common Problems

Following are some common drawbacks faced by Indian iron and steel industry:

- The industry requires large capital investment which a developing country like us cannot afford. Many of the public sector integrated steel plants have been established with the help of foreign aid and are running with obsolete technology.
- During the last two decades after the oil crisis, steep hike in energy costs and escalation of costs of other inputs, reduced the margin of profit of the steel plants. This resulted in lower enthusiasm among investors to invest in steel sector thus hampering process of technological-up gradation.
- Indian plants are running on obsolete technology using coal where as the new technological developments in countries such as Iran, Saudi-Arabia and Mexico facilitates the use of natural gas and iron ore to make direct reduced iron ensuring better material value productivity, higher end product recovery and low carbon emissions.
- Material value productivity in India is still very low. In Japan and Korea, less than 1.1 tonnes (and in several developed countries 1.05 tonnes) of crude steel is required to produce a tonne of saleable steel. In India, the average is still high at 1.2 tonnes.
- The per capita labour productivity in India is at 90-100 tonnes per year which is one of the lowest in the world. The labour productivity in Japan, Korea and some other major steel producing countries is about 600-700 tonnes per man per year. At Gallatin steel, a mini mill in the U.S., there are less than 300 workers to produce 1.2 million tonnes of hot-rolled coils. A comparable firm in India employs 5,000 workers.
- Raw material scarcity is on the top of the agenda. India is very dependent on imported coking coal. Approximately 60-65 per cent of the domestic coking coal requirements are met through imports due to unavailability of appropriate quantities in the country.

Suggestions

- India needs both public as well as private investments in urban and rural infrastructure, real estate, roads, railways, civil aviation and irrigation to boost-up consumption of steel.
- Given the fact that steel market across the globe is vulnerable to global conditions, India needs to be more proactive in diversifying its export markets. It could, therefore, adopt a similar strategy as Brazil, focusing on geographical nearer markets where it has a freight advantage, such as Nepal, Bangladesh, Sri Lanka and Middle-East.

- Indian companies should target export destinations for steel sheet products, such as the Middle East and Africa, where they have a freight advantage over China, Japan and South Korea.
- India, through make in India campaign, attract investment in focal areas such as automobiles, auto-component, defence-equipment, engineering goods, plant and machinery thus using Indian steel in manufacturing of 'value-added products'. It will ensure sustainable development of Indian industry and protect it from vagaries of sudden price changes in steel in international markets.

Answer 1(c)

FTAs are arrangements between two or more countries or trading blocs that primarily agree to reduce or eliminate customs tariff and non tariff barriers on substantial trade between them. This is to help the two trading countries to identify certain products for tariff liberalisation pending the conclusion of FTA negotiation. It is primarily a confidence building measure. FTAs, normally cover trade in goods (such as agricultural or industrial products) or trade in services (such as banking, construction, trading etc.). FTAs can also cover other areas such as intellectual property rights (IPRs), investment, government procurement and competition policy, etc. Early harvest scheme (EHS) is a precursor to a free trade agreement (FTA) between two trading partners. The EHS has been used as a mechanism to build greater confidence amongst trading partners to prepare them for even bigger economic engagement. A good example of an EHS is between India and Thailand signed in October 2003, wherein 83 products were identified to be reduced to zero in a phased manner.

Domestic steelmakers have urged the government to keep steel out of the purview of any future free-trade agreements (FTAs) and also review the existing pacts to ensure that their interests are safeguarded. Taking the advantage of the duty benefits under FTAs steelmakers from Japan and Korea have already become a serious threat to Indian steel industry.

Answer 1(d)

The Government of India has taken this matter seriously by implementing following steps not only to protect and but also to develop the industry.

- It imposed a 20 per cent ad valorem safeguard import duty on some steel products.
- It also set a floor price or minimum import duty (MIP) on 173 steel products to deter countries led by China from undercutting local mills-the first such move in more than 15 years. Due to this, the import became costlier by 26-70 per cent helping the local steel players to compete better.
- Further it is imposed anti-dumping duty on stainless steel imports, as it tries to protect the struggling domestic industry from cheap imports. Some other countries have also adopted the same practices like America and Australia has imposed dumping duties on Chinese steel, India steelmakers may attract anti-dumping duty in Canada also.
- Out of the nearly two dozen sectors identified by the government as focus areas under the 'Make in India' campaign, the cost of steel is crucial to the

competitiveness of manufacturing in at least nine industries-automobile, automobile components, construction, defence manufacturing, electrical machinery, railways, renewable, thermal power, and oil and gas.

- Additionally, the government's focus on rural-urban (rurban) cluster development is also likely to push up demand for steel. The budget outlay of Rs. 221246 crore on infrastructure including railways meets a long standing demand from core sectoral industries such as cement and steel.
- For ensuring quality of steel several items have been brought under a quality control order issued by the Government.

Answer 1(e)

Dumping is said to occur when goods are exported by one country to another country at a price lower than the normal value of the goods. This is an unfair trade practice which can have a negative impact on international trade. Often, dumping is mistaken and simplified to mean cheap or low priced imports. Whereas anti dumping is a measure to rectify the situation arising out of the dumping of goods and its negative international trade effects. Thus, the purpose of anti dumping duty is to rectify the negative trade-effect of dumping and re-establish fair trade. The use of anti dumping measure as an instrument of fair competition is permitted by the WTO.

India imposed anti-dumping on stainless steel imports, as it tries to protect the struggling domestic industry from cheap imports from China. Some other countries have also adopted the same practice like America and Australia and have imposed dumping duties on Chinese steel, Indian steelmakers may attract anti-dumping duty in Canada etc.

The Indian steel industry is expected to face following global challenges till 2025 and beyond:

- Australia and Brazil are expected to supply about 90 per cent of all seaborne iron ore by 2022. This increase in supply and moderation in demand may continue to expert pressure on iron-ore prices.
- China, which is currently a net importer of scrap, is expected to have a surplus of scrap by 2025. This will decrease demand and push-down the prices of other raw materials such as coking coal and iron ore.
- Shale gas emerging as cheap source of energy could change the competitive landscape in steel making. Countries such as Iran, Saudi Arabia and Mexico are using natural gas and iron ore to make direct reduced iron (DRI). This process does not need coking coal.
- Ongoing research in the steel industry, especially to meet the environmental standards, will bring in a lot of technological changes in coming years which are quite expensive.

Question 2

(a) India is currently the ninth largest civil aviation markets in the world. It is projected to be the third largest aviation market by the year 2020. Using Michael Porter's five forces model to the industry, discuss :

(i) Threats of new entrants

(ii) Competitive rivalry among current players. (5 marks)

(b) Why do countries form regional trading blocks ? Do regional trading blocks help or hurt world trade ? (5 marks)

(c) Your friend is planning to start business as merchant exporter of gems and jewellery items. Being an international business consultant, prepare a note advising your friend on details of 'export from India scheme'. (5 marks)

(d) Which transitional arrangements are available for an exporter in the Foreign Trade Policy 2015-20 ? (5 marks)

(e) Explain the functions of the Export Promotion Council and the procedure for obtaining registration-cum-membership certificate of this Council. (5 marks)

(f) How does adoption of information technology in warehousing increase competitiveness ? (5 marks)

Answer 2(a)

The Indian aviation sector has witnessed tremendous growth in the recent past which is driven by sound demographic, macroeconomic and market dynamics. The three fold increase in consumerism, rising disposable income; booming aviation sector; proliferating middle class; increasing business travel; government reforms; entry to low cost carriers; increasing competition etc have positioned in Indian aviation sector in a high growth trajectory. At present, India is one of the fastest growing aviation markets in the world with a passenger traffic stood at 163.06 million during 2013. The country is projected to be the 3rd largest aviation market by 2020.

(i) Threat of New Entrants

- Aviation industry needs substantial investments at the entry level as also at the operating level; and this warrants intensive capital-outlay which constitutes the biggest barrier of entry for the new players.
- The regulatory approvals and licensing is also an important deterrent for the new entrants into the aviation industry.
- Advanced operating acumen for labour in skilled positions such as pilots, aircraft maintenance engineers, technicians and in-flight crew is the call of the aviation whereby a high learning curve is charted.
- Superior technology forms the base line of aviation anywhere and everywhere in the world. Inventions and technological up-gradations keep hopping uninterrupted.
- Beak-even period in aviation industry are longer and only those entrants, who has deep-pockets of revenue stream from other sources can survive in this industry.
- Upward changes in oil prices can bring down even an established player in the market, thus investor and entrants thinks many times before entering into civil aviation industry.

(ii) Competitive Rivalry among Current Players

- The airline industry functions in an intense competitive market of cut-throat fares. Put it across, competition in aviation sector is severe amongst the

rivals. Customer luring is resorted to by the competitors through a raft of ancillary services and low prices which are, in turn, leading to lower and lower margins.

- Multiple airlines keep-on competing with each other with lucrative offers relating to the pricing of tickers, frequent flier programmes, loyalty programs, etc., with a view to attract and retain the customers.
- The existing players of the industry are prone to high exit barriers, mainly due to its specialized equipment with little or no alternative uses.
- Custom service is key to success in aviation industry. There is intense competition among various players to outpace each other on this front. They have to spend a lot on training of their personnel on issues such as etiquettes, dressing, and punctuality-reward program, motivation, morale-boosting, team-building and de-stressing programs of their employees.

Answer 2(b)

Economic integration among countries is the order of the day. Prime motivations for forming the regional trading blocs are access of newer markets at zero tariff, elimination of non-tariff barriers, more investment and employment opportunities, higher economic growth and increased gross domestic product, secure borders and stronger political ties emanating out of these economic engagement thus reducing the scope for war and political other threats.

Firms, in the initial stage of internationalization, must be aware of the regional groups that encompass countries targeted for manufacturing locations or market opportunities. As firms proceed towards greater multi-nationalism, they need to change their organizational designs and operating strategies to take advantage. The split of cooperation was designed to promote economic growth and stability. Trade diversion occurs when trade is diverted from countries outside the trading area to countries inside. This results from the removal of tariffs and other barriers in the trading area, making it cheaper or easier to export to or import from these countries. External countries will find it especially difficult to retain their export markets if the common external tariff is higher than the previous importing country's tariff. In such a case, trade division may not be beneficial as trade may be diverted from a more efficient producer outside the trading area to a less efficient one inside.

Generally, there will be gainers and losers from trade diversion- the net gain or loss will depend on the particular circumstances. The entry of Spain into the European Union provides an interesting example of trade creation and diversion. It is the duty of policy makers and negotiators to look-after the areas of mutual benefits while giving and taking on negotiation fronts with partner countries.

Answer 2(c)

The foreign trade policy 2015-2020 highlights following important guidelines on the export of gem and jewellery from India to abroad.

Before Starting Gems and Jewellery Business: Planning Stage

- He must have Importer-Exporter Code issued by Director General of Foreign

Trade as he can export or import only with this license. It can be availed by filing ANF- (online) along with copy of pan card, address proof, cancelled cheque, online payment of Rs. 500/- and applicable registration (for example partnership deed in case of partnership firm or CIN detail in case of company).

- He must have Registration Cum Membership Certificate issued from Gems and Jewellery Export Promotion Council.
- Additionally, he must have Excise Control Code as Gems & Jewellery is now excisable products to neutralize the incidence of excise (against ARE- 1 or ARE-2). He should also have Service Tax registration to neutralize the incidence of Service Tax (at output stage) and finally he must have VAT and CST registration for neutralization the incidence of VAT or CST (as the case may be).
- He must ensure that he source diamonds from any source only with "Kimberly Certification" failing which he cannot export gems and jewellery to anywhere as it is mandated under FTP against Security Council Resolution of 2004.

At The Time of Export

- Items if exported will be eligible for export are gold jewellery, including partly processed jewellery and articles including medallions and coins (excluding legal tender coins), whether plain or studded, containing gold of 8 carats and above;
- Items eligible for export silver jewellery including partly processed jewellery, silverware, silver strips and articles including medallions and coins (excluding legal tender coins and any engineering goods) containing more than 50% silver by weight;
- Items eligible for export are platinum jewellery including partly processed jewellery and articles including medallions and coins (excluding legal tender coins and any engineering goods) containing more than 50% platinum by weight;
- Replenishment authorization for Gems may be issued against export including that madeagainst supply by Nominated Agency and against supply by foreign buyer;
- Four Star Export House from Gems & Jewellery sector may be recognized as Nominated Agency by regional authority;
- Reserve Bank of India can authorize any bank as Nominated Agency. Procedure for import of precious metal by Nominated Agency (other than those authorized by Reserve Bank of India and the Gems & Jewellery units operating under EOU and SEZ schemes) and the monitoring mechanism thereof shall be as per the provisions;
- A bank authorized by Reserve Bank of India is allowed export of gold scrap for refining and import standard gold bars as per Reserve Bank of India guidelines.

The Gem and Jewellery Export Council (GJEPC) has over the years effectively monitoring the scattered efforts of individual exporters to make this sector a powerful engine driving India's export-led growth.

Answer 2(d)

- License / Authorisation / Certificate / Scrip / any instrument bestowing financial or fiscal benefit issued commencement of FTP 2015-20 shall continue to be valid for the purpose and duration for which such License / Authorisation / Certificate / Scrip / any instrument bestowing financial or fiscal benefit Authorisation was unless otherwise stipulated.
- An export or import that is permitted freely under FTP is subsequently subjected to any restriction or on, such export or import will ordinarily be permitted, notwithstanding such restriction or regulation, otherwise stipulated. This is subject to the condition that the shipment of export or import is made within final validity period of an irrevocable commercial letter of credit, established before the date of imposition restriction and it shall be restricted to the balance value and quantity available and time period of such able letter of credit. For operationalising such irrevocable letter of credit, the applicant shall have to the Letter of Credit with jurisdictional Regional Authority (RA) against computerized receipt, within 15 the imposition of any such restriction or regulation.

Answer 2(e)

The major functions of the Export Promotion Council (EPC) are as follows:

- To provide commercially useful information and assistance to their members in developing and increasing their exports
- To offer professional services to its members in various areas
- To organize visit of delegation of its members abroad to explore overseas market
- To organize participation in trade fairs, exhibitions and buyer-seller meets in India and abroad etc.
- Interaction between the exporting community and both centre and state government.

Registered under the Indian Company Act, Export Promotion Council is a non-profit organization for the promotion of various goods exported from India in international market. EPC works in close association with the Ministry of Commerce and Industry, Government of India and act as a platform for interaction between the exporting community and the government. So, it becomes important for an exporter to obtain a Registration cum Membership Certificate from the EPC. An application for the registration should be accompanied by a self certified copy of the IEC (provided by the Director General of Foreign Trade) number. Membership fee should be paid in the form of cheque or draft after ascertaining the amount from the concerned EPC. The RCMC certificate is valid from 1st April of the licensing year in which it was issued and shall be valid for five years ending 31st March of the licensing year, unless otherwise specified.

Answer 2(f)

Today the role of technology has transformed from being an enabler of productivity and quality through process automation and quality control to a more strategic role as a key influencer of competitive advantage. The last decade of the 20th century has

witnessed rapid technological advances, especially in IT. Increase in IT adoption and knowledge infrastructure can provide a boost to the growth and maturity of warehousing players in India. IT has today presented enterprises with possibilities of delivering substantial operating savings while at the same time improving the quality of order fulfilment. India's warehousing technology market in India is growing steadily, with the upswing in demand from the thriving logistics, retail and manufacturing sectors, as well as government promotion. As the booming manufacturing and retail sectors are the main users of these technologies, sustained demand from these areas is ensured. For instance, Wal-Mart has made it mandatory for its suppliers to deploy Radio Frequency Identification ('RFID'). In fact, three technologies, bar coding, RFID and Global Positioning System has redefined the logistics industry including management of warehouses. A warehouse keeper can track any packet or carton anywhere in the warehouse by using RFID technology and any specific packet or item within container or carton by using bar-coding technology. Bar coding ensures fool proof stock-keeping and inventory management. Global positioning system can help a warehouse keeper to plan in advance for arriving cargo if any and outside moving cargo if any by tracking the carriers involved in transportation such as ships, aircraft, truck and rail. The growth of India as a major sourcing nation for the world's leading retailers is also ramping up demand.

Until recently, the logistics industry was highly unorganised, comprising predominantly medium and small-sized Layered Service Providers ('LSPs'). However, the trend is changing with the increase in the number of organised LSPs and improvement in the services offered by them through 3PLs and 4PLs. To obtain the cutting edge in the market, logistics and dedicated warehousing companies are adopting these technologies to improve warehousing and supply chain management. This enables them to achieve maximum warehousing efficiency.

Question 3

Economies of certain countries are dependent mainly on international trade. Discuss. *(5 marks)*

Answer 3

Today hardly is there any country which is not engaged in International Trade. The economies of certain small countries are dependent mainly on International Trade. There are a number of factors which contribute to the development of foreign trade. Most important among them are:-

1. *Natural Resources and Geographical Factors* : Each country differs in natural resources and geographical distribution of various factors of production. Diversities in natural and geographical conditions make a country more efficient in the production of one commodity and another country in some other commodity. These countries specialise themselves in the production of such commodities and supply them to other countries in exchange for the commodities which they do not produce but other countries have specialisation in their production. For example, because of favourable natural conditions, India and Sri Lanka taken together produce 87% of the world total production of tea. Mica in India, manganese in Russia and oil in Arab countries are a few examples of this kind of specialisation.

2. *Occupation Distribution* : The population and its occupational distribution also

differ from country to country. Occupational structure of its population decides the field of specialisation. For example, a large part of India's population is engaged in agriculture, hence it has specialised in the production of food grains and other agricultural products. England, on the other hand, has specialised itself in the production of Industrial goods as it has abundance of capital and scarcity of land and a large part of its population is engaged in Industries. Thus, countries specialise themselves on the basis of their occupations. Specialisation gives birth to international trade.

3. *Means of Transport* : Means and costs of transportation also contribute to the International trade. Industries using weight losing raw materials, one generally localised at places near to the raw materials because the transport costs is the deciding factor. The countries where such raw materials are found in abundance, get specialised in their end-product. For example, India is a large producer of sugarcane and therefore, sugar industry is located mainly in India. At International level, the factors of production are not freely movable, because they involve high cost of transportation. Other countries, therefore cannot set up sugar industries and shall make imports of sugar from India and other sugar producing countries.

4. *Large-scale Production* : Large scale production of a commodity gives many advantages of scale. The industry of such a commodity can produce it at a lower cost because of scale economics and specialisation. After meeting the demand for the commodity in the national market, the surplus can easily be exported at a price fetching and handsome profits to the industry. For example, an industrial unit producing locomotive engines for the Indian Railways, can specialise itself in the production of locomotives. Large scale production of locomotives may enable the unit to export them to neighbouring countries.

5. *Differences in Costs* : Production costs of a commodity differ from country to country due to a number of factors like Availability of natural resources and geographical conditions, Occupational structure, Large-scale production, Development in the field of science and technology etc. Countries having favourable conditions can produce the commodities at lower costs and other countries at higher costs. Higher domestic costs of production shall encourage the imports of that commodity into the country and lower costs items may be exported.

6. *Degree of Self-sufficiency* : No country of the world is self-sufficient. The degree of self-sufficiency however differs from country to country. For example the Russia imports 2% to 3% of its requirements and the USA only 4% to 5% of its total consumption. The degree of self sufficiency is 40% to 50% in underdeveloped countries. Therefore, the countries which cannot produce at all or can produce only at a very high cost, arrange the supply of such goods through imports from other countries.

Question 4

Describe main modes of FDI with strategic alliance. Highlight the mode widely operational in India. *(5 marks)*

Answer 4

The three main modes of FDI with strategic alliances are (a) Mergers and Acquisitions or M&A and (b) Joint Venture or JV and (c) Green Field Investments.

Mergers and acquisitions (M&A) are transactions in which the ownership of companies, other business organizations or their operating units are transferred or combined. As an aspect of strategic management, M&A can allow enterprises to grow, shrink, change the nature of their business or improve their competitive position. From a legal perspective, a merger is a legal consolidation of two entities into one entity, whereas an acquisition occurs when one entity takes ownership of another entity's stock, equity interests or assets. International M&A are growing day by day. These are also known as cross-border M&A. It is occurring in various dimensions like horizontal mergers, vertical mergers, concentric mergers, conglomerate mergers, reverse mergers, dilutive mergers, accretive mergers etc. These are performed for the purpose of obtaining strategic advantages like scale economies and also stimulate FDI.

A joint venture (JV) is a business entity created by two or more parties to undertake economic activities together, generally characterized by shared ownership, shared returns and risks, and shared governance. Key elements of a joint venture's design include: 1) the number of parties; 2)the geographic, product, technology and value-chain scope within which the JV will operate; 3) the contributions of the parties; 4) the structural form 5) the valuation of initial contributions and ownership split among the parties; 6) the economic arrangements, post-deal; 7) governance and control; 8) Talent/HR model; 8) contractual arrangements with the parent companies for inputs, outputs or services; 9) exit and evolution provisions.

Wholly Owned Subsidiary or green field investment is a form of foreign direct investment where a parent company builds its operations in a foreign country from the ground up. In addition to the construction of new production facilities, these projects can also include the building of new distribution hubs, offices and living quarters. These projects are foreign direct investments that provide the highest degree of control for the sponsoring company. In these projects, the company’s plant construction is done to its own specifications, employees are trained to company standards and fabrication processes can be tightly controlled. This type of involvement is completely different than indirect investments, where companies may have little or no control in operations, quality control, sales and training. As a long-term commitment, one of the greatest risks in green field investment is the relationship with the host country. Any circumstances or events that result in the company pulling out of a project at any time can be financially devastating. In April 2015, Toyota announced its first green field project in Mexico in three years, a $1.5 billion manufacturing plant in Guanajuato. The factory is scheduled to open in 2019 with 2,000 employees and capacity to produce 200,000 cars per year.

Out of these three modes, green field investment has the most preferred and widely operational mode of foreign direct investment in India.

Question 5

A small Indian firm has developed some valuable new medical products using its unique biotechnology know-how. It is now trying to decide how to best serve the

markets of USA, Russia and Brazil and has identified the following options for consideration :

(i) Manufacture the product at host country and appoint foreign sales agents to manage marketing activity.

(ii) Manufacture the product at host country and set-up a wholly owned subsidiary in each country to manage marketing.

(iii) Enter the respective countries by alliance mode with pharmaceutical firms operating in the countries. The medicine would be manufactured in each respective country by 50/50 joint venture and the respective foreign firms would take the responsibility of making medicine in their own country.

If investment in medicine manufacturing facilities is a major criteria, choose the best option, giving reasons. (5 marks)

Answer 5

Since investment is a major criteria in leveraging business model first appointing a sales agent second setting up the wholly owned subsidiary in each country and third entering into strategic alliance through joint venture.

Market USA : It is recommend to small firms to enter into strategic alliances with local partner in United states to sell such newly developed bio-technology products as local partner, with his previous exposure to US market, can help in all regulatory clearances from various authorities. As US has very strong compliance through USFDA, it will be appropriate to manufacture through joint venture thus eliminating scope for consignment basis clearance for each export orders. More so, Indian manufacture is still a small firm thus can bank on capital investment of foreign joint venture partner. More so, distribution is an important element in sales of bio-tech product and Indian small firm can bank upon or piggyback on distribution infrastructure and experience of his joint venture partner.

Market Russia : Russia is an important market for bio-technology products but has witnessed a declining trend in population after disintegration from USSR. Regulatory compliance is strict and language is an important barrier for Indian small exporter. Russia trade regime is also not that transparent as it become member of WTO only in recent year and there is presence of oligarch in the pharma market with policy maker still having a mind-set of communism. Under these circumstances, it is recommended not to invest too much capital and obvious option will be to appoint to a local sales agent for catering to requirement of bio-tech products in Russia.

Market Brazil : Brazil is an important and growing market for biotech product. Being into southern hemisphere, there is great similarities in nature of diseases prevent in India and Brazil. It is member to largest trading bloc in Southern America namely 'Mercosur' thus having free trade opportunities with countries such as Venezuela, Uruguay, Paraguay, Argentina etc. A Wholly owned subsidiary shall be best investment decision for this small firm Brazil offer great opportunities in terms of market size, future growth, similarity in nature of usage, low competition, non-presence of established player, scope for expansion as Brazil offer a great opportunities to trade with neighbouring countries of Latin America. It is recommended for small firm to get into Brazil with Wholly Owned Subsidiary model.

Question 6

It has been argued by experts that agreements on anti-dumping practices and agreement on subsidies and countervailing measures are defensive tools available to importing countries to deal with conditions of unfair trade practices in international trade. Do you agree ? Justify. *(5 marks)*

Answer 6

Dumping is said to occur when the goods are exported by a country to another country at a price lower than its normal value and this causes injury to domestic industry. This is an unfair trade practice which can have a distortive effect on international trade as it keeps competitors out of a particular market. Anti dumping measures rectify the situation arising out of the dumping of goods and its trade distortive effect. The use of anti dumping measure as an instrument of fair competition is permitted by the WTO. The WTO Agreement on implementation of Article VI of GATT (Anti dumping Agreement) lays down that injury can be material injury to a domestic industry, threat of material injury or material retardation of the establishment of such an industry. Anti dumping duty is recognised as an instrument for ensuring fair trade and is not a measure of protection per se for the domestic industry. It provides relief to the domestic industry against the injury caused by dumping. On the other hand, WTO Agreement on Subsidies and Countervailing Measures (ASCM) sets out the remedies, which WTO Members have against injurious subsidization and the procedures, which they must follow. It provides detailed rules on the concepts of subsidization, actionable subsidies and material injury/ serious prejudice. It contains many procedural provisions that WTO Members, wishing to take countervailing duty action (the unilateral track), must comply with. It also provides provisions for attacking certain subsidies in the WTO (the multilateral track).

An important aspect of the current framework of disciplines on subsidies is that India together with other low-income countries has been exempted from the prohibition on export subsidies for non-agricultural products. However, this exemption does not imply immunity from countervailing duty procedures, if the subsidised products cause material injury to domestic industries in importing countries. Consequently, while Indian exports have benefited from export incentives in some destinations, the importing countries have countervailed against these incentives. Indeed, some export incentives given in India are countervailable in terms of the SCM Agreement. Similarly other countries also use anti-dumping as an instrument to control the unwanted imported of “dumped” products. WTO framework accepts these to be defensive tools for importing countries so as to ensure orderly and fair development of international trade.

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