
EVOLUTION OF SERIOUS FRAUD INVESTIGATION OFFICE AND ITS WORKING

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ABSTRACT

This research deals with the evolution and the working of Serious Fraud Investigation Office (SFIO) established under the Ministry of Corporate Affairs of the Government of India as per the provisions of the Companies Act, 2013. The research aims to explain the pressing need for a specialised agency such as the SFIO to deal with the complex corporate frauds which are beyond the capabilities of a regular investigating agency to resolve and make liable the culprits of the economic frauds.

With the globalisation and advancement of the technology, the complexities of the corporate world have also increased. In contrast with the earlier frauds, the scams and malpractices in the corporate world are not just restricted to a particular field, but have several facets which cannot be easily detected. In order to understand the nature of frauds and to fulfil the gaps, specialists from different fields are required to work together. The establishment of the SFIO can be said to be in the right direction which has taken consideration of this issue. SFIO comprises of members who are experts in different fields such as financial sector, capital market, accounting, forensic auditing, taxation, law, information technology, business law, customs, etc.

This study focuses on the power of the SFIO and the procedure followed by it in the investigation of the matters referred to it by the central government. It is necessary to analyse the power and procedure of the agency so that it can be understood whether there is any lacking or there is a need for the enhancement of the functions of the SFIO, so that it can tackle corporate frauds more efficiently.

INTRODUCTION

Under the Ministry of Corporate Affairs of the Government of India, the Serious Fraud Investigation Office (SFIO) has been established as a multidisciplinary agency comprising of members from different fields such as finance, capital market, accounting, forensic audit, taxation, law, information technology, business law, customs, etc. It was recommended by the Naresh Chandra Committee, which was set up in 2002 to examine various aspects of corporate governance and suggest reforms. The purpose of the Committee was to examine how the Company Law Board operated and make recommendations for improvements. Based on the recommendation, it was established in July 2003.

Serious Fraud Investigation Office is an organization in India that investigates serious fraud cases involving complex issues which extends to various fields and need careful and detailed investigation. The Ministry of Corporate Affairs of the Government of India is in charge of it. It is a multidisciplinary organization with professionals from the financial sector, capital market, accounting, forensic audit, taxation, law, information technology, business law, customs, and experts to prosecute white-collar crimes and frauds under the company's law. The agency's headquarter is in New Delhi. This was a key recommendation of the Naresh Chandra Committee on Corporate Governance, which was established by the government on August 21, 2002. On January 9, 2003, the government approved the formation of the organization. The Companies Act of 2013 provides statutory support for the SFIO, which had originally been founded as a non-statutory organization.

HISTORICAL BACKGROUND

Financial and corporate fraud have devastating impacts on a variety of stakeholders, the general public, and the overall economy of the nation. In order to present themselves in the best possible light, firms frequently strive to build a "rosy" picture of their financial situation. This becomes much easier for them as they have teams of experts from different background who are well trained in their respective fields. As a flourishing business, they use a variety of dishonest and unethical methods to window dress their finances and give the stakeholders a false impression. It is very challenging to detect corporate frauds and make liable the persons actually responsible for it,

because the persons involved in it are experts in their own fields and there are various angles that needs to be analysed and carefully investigated before a fraud can be uncovered. Increased corporate frauds not only demotivate the investors from investing in a business but it also affects negatively the foreign investment in the country. Ease of doing business rank also decreases which ultimately hampers the overall economy of the nation. Therefore, the need for a specialized investigation agency was needed because the existing agencies like CBI and other agencies did not have expert members to investigate the corporate frauds involving deep technicalities.

The Central Government had the power to look into corporate frauds even though the Companies Act of 1956 did not explicitly include provisions for the SFIO. This included looking into a company's operations, affiliate companies, and ownership. The Companies Act of 1956 permitted the appointment of inspectors by the Central Government based on recommendations from the Registrar or the Company Law Board prior to the SFIO receiving formal recognition in 2003. Only if it served the public's or shareholders' interests, and not their own, could these inspectors look into and report on a company's activities that were fraudulent or illegal.

As time went on, several nations liberalized their economies and removed obstacles to the creation of multinational corporations. In an effort to maximize profit and revenue, companies use dishonest and misleading practices that ultimately causes loss to the investors. In view of the different corporate scams worldwide, the Indian government, in 2002 formed a committee headed by Naresh Chandra to examine and recommend ways to enhance corporate governance.

“The Government in the backdrop of major failure of non-banking financial institutions, phenomenon of vanishing companies, plantation companies and the recent stock market scam had decided to set up Serious Fraud Investigation Office (SFIO), a multi-disciplinary organization to investigate corporate frauds. The Organization has been established and it has started functioning since 1st October, 2003.”¹

A statutory corporate fraud investigation agency, the SFIO is overseen by officers from the Indian

¹ Ministry of Corporate Affairs,
https://www.mca.gov.in/mca/html/mcav2_en/home/aboutmca/affiliatedoffices/seriousfraudinvestigationoffice/sfio.html#:~:text=The%20Government%20in%20the%20backdrop,organization%20to%20investigate%20corporate%20frauds, (Last visited on September 5,2023)

Administrative Service, Indian Revenue Service, Indian Police Service, Indian Corporate Law Service, and other Central Services. It falls under the purview of the Ministry of Corporate Affairs (the "MCA"). It was established as a result of a resolution that the Indian government approved on July 2, 2003. On the proposal of the Naresh Chandra Committee on Corporate Governance, which was established in the wake of stock market scandals, the Vajpayee Government chose to establish SFIO.

The inquiries were conducted by the SFIO in accordance with sections 235 to 247 of the Companies Act of 1956. Using professionals from a variety of industries, including the financial sector, forensic audit, taxation field, legal field, capital market, accountancy, information technology, customs, and other pertinent areas, the SFIO conducts multidisciplinary investigations of corporate frauds cases handed over to it by the central government. These experts typically come from a variety of institutions, including banks, the Securities and Exchange Board of India, the Comptroller and Auditor General Office, and other relevant institutions and government agencies. Its regional offices are located in Mumbai, Kolkata, Chennai, and Hyderabad. The Agency's headquarters are in New Delhi.

SFIO did not have a formal legal status at first as there was no mention of it in the earlier Companies Act. According to sections 235 to 247 of the former Companies Act of 1956, it conducted investigations into the suspected frauds acting as an executive agency for the Central Government or a Court of Competent Jurisdiction within the confines of the law. Although several SFIO officers have been given permission to file complaints against defaulting corporations under Section 621 of the Companies Act, 1956 (as persons approved by the Central Government), the SFIO is not specifically mentioned in the Act. It was only after the passage of the 2013 Companies Act that the SFIO received Statutory recognition. The 2013 Act added Section 447, which, for the first time, offered a definition of fraud as well as punishment for such an offence. This was done to tackle the rising number of corporate fraud cases in India. The 2013 Act's inclusion of this extremely broad definition of fraud, which combines several provisions of the Indian Penal Code (the "IPC"), appears to have been primarily motivated by the Satyam scam, Ketan Parekh Scam and a few other corporate scandals that emerged during the time when the 2013 Act was being considered by Parliament.

“According to s.211 of The Companies Act, 2013:

(1) The Central Government shall, by notification, establish an office to be called the Serious Fraud Investigation Office to investigate frauds relating to a company:

Provided that until the Serious Fraud Investigation Office is established under subsection (1), the Serious Fraud Investigation Office set-up by the Central Government in terms of the Government of India Resolution No. 45011/16/2003-Adm-I, dated the 2nd July, 2003 shall be deemed to be the Serious Fraud Investigation Office for the purpose of this section.

(2) The Serious Fraud Investigation Office shall be headed by a Director and consist of such number of experts from the following fields to be appointed by the Central Government from amongst persons of ability, integrity and experience in, --

(i) banking;

(ii) corporate affairs;

(iii) taxation;

(iv) forensic audit;

(v) capital market;

(vi) information technology;

(vii) law; or

(viii) such other fields as may be prescribed.

(3) The Central Government shall, by notification, appoint a Director in the Serious Fraud Investigation Office, who shall be an officer not below the rank of a Joint Secretary to the Government of India having knowledge and experience in dealing with matters relating to corporate affairs.

(4) The Central Government may appoint such experts and other officers and employees in the Serious Fraud Investigation Office as it considers necessary for the efficient discharge of its functions under this Act.”²

INVESTIGATION

“Section 212³ : Investigation into affairs of company by Serious Fraud Investigation Office.

(1) Where the Central Government is of the opinion, that it is necessary to investigate into the affairs of a company by the Serious Fraud Investigation Office--

(a) on receipt of a report of the Registrar or inspector under section 208;

(b) on intimation of a special resolution passed by a company that its affairs are required to be investigated;

(c) in the public interest; or

(d) on request from any Department of the Central Government or a State Government,

the Central Government may, by order, assign the investigation into the affairs of the said company to the Serious Fraud Investigation Office and its Director, may designate such number of inspectors, as he may consider necessary for the purpose of such investigation.”

From the provision it is clear that the Central Government has a discretionary power to order investigation by SFIO. Under Section 210(2) is a requirement that stipulates the Central Government "shall" order an investigation into the company's operations when a court or tribunal issues a ruling to this effect. But, the case with s.212 is different. The central Government, as regards the investigation by SFIO has complete discretion. It is only after forming “opinion” the Central Government can order investigation into the affairs of a company by SFIO. The legislature has given heavy weightage to the opinion of the Central Government and from the provision, the

² The Companies Act, 2013, § 211, No. 18, Acts of Parliament, 2013 (India)

³ The Companies Act, 2013, § 212, No. 18, Acts of Parliament, 2013 (India)

intention of the legislature is evident that any investigation ordered without “forming opinion” would be open to challenge. It can also be argued that the undue weightage to the opinion of the central government is somewhat a hindrance to the objective of the provision. There may be circumstances when the fraud can be tackled during its infancy but due to the requirement of the provision, there would be unnecessary delay in the investigation.

No other investigating agency of the Central Government or any State Government may investigate a case in which the Serious Fraud Investigation Office has been given the assignment to conduct an investigation under the Act. If such an investigation has already been started, it shall not be continued, and the concerned agency shall transfer the pertinent documents and records to the SFIO. The provisions are clear that the SFIO will have the sole jurisdiction to investigate a matter handed over to it and no other agency will interfere in any manner in its working. The SFIO has been given utmost freedom in these matters. This is also necessary keeping in view the complexities of the matters which if not carefully handled may defeat the whole purpose of setting up a specialized agency.

According to Section 212(3), the SFIO must undertake the investigation and submit its report within the time frame provided in the Central Government order when the inquiry into a company's operations has been handed over to it by the Central Government. However, the 2013 Act does not provide a deadline for the SFIO to finish the inquiry and submit the investigation report. By itself, Section 212(3) of the 2013 Act does not provide a deadline for submitting the report. Again, there is no time limit specified under sub-Section (12), which is about "investigation report". In fact, a report of this kind is to be produced in accordance with sub-Section (12) "upon completion of the investigation". In accordance with standard legal standards, there is no requirement for the investigation to be completed within a specific time frame.

“In Section 212(3) of the 2013 Act, the word "assign" itself refers to a transfer of an investigation for all purposes, after which the original investigating agencies of the Central Government or any State Government loses all authority to conduct and complete the investigation in regard to the offences mentioned therein. Complete transfer of the investigation is the concept outlined in sub-Section (2). The transfer made pursuant to Section 213 (2) would not be affected by any eventuality. The provisions should have addressed what happens if the time restriction is not

followed if a time limit is intended and considered within which the investigation must be completed. The Statute must have also anticipated the requirement that any legitimate investigation conducted by a Central Government or State Government Investigating Agency that was transferred to SFIO be returned to those Investigating Agencies. The Statute, however, does not allow for that. The transfer cannot be undone in any way; it is final. After being assigned, SFIO retains the authority to carry out and finish the investigation.” This was observed by the Supreme Court of India in “*Serious Fraud Investigation Office v. Rahul Modi*”⁴. It was held that the time-period specified in the order is only directory, and not mandatory. The authority to investigate shall not end once the time-period specified by the Central Government has been extinguished.

According to s.212(4), the director of the Serious Fraud Investigation Office shall cause the matter to be investigated by an Investigating Officer who will have all the powers of the inspector under section 217 to look into the company's business. The corporation, its officers, and any employees who are currently or have previously had worked with the company are accountable and duty bound for giving the investigating officer any and all information, justifications, documents, and help he may need to carry out the investigation.

If any officer, not below the rank of Assistant Director of Serious Fraud Investigation Office, authorized in this capacity by the Central Government by general or special order, has reason to believe that any person has been guilty of any offence punishable under the sections mentioned in subsection (6) on the basis of material in his possession, he may arrest that person and shall, as soon as possible, inform him of the ground. The officer is required to send a copy of the order to the Serious Fraud Investigation Office in a sealed envelope as soon as the person is arrested, and the Serious Fraud Investigation Office is required to retain the order and material for the length of time that may be prescribed. Every person arrested under shall within twenty-four hours, be taken to a Special Court or Judicial Magistrate or a Metropolitan Magistrate, as the case may be, having jurisdiction. However, the provisions relating to arrest were made effective only in 2017.

Serious Fraud Investigation Office shall send an interim report to the Central Government upon request from the Central Government. The Serious Fraud Investigation Office must submit the

⁴ *Serious Fraud Investigation Office v. Rahul Modi*, (2019) 5 SCC 266

investigation report to the Central Government after the inquiry is complete. A copy of the investigative report may be received by any interested party by making a court application.

Following review of the investigation report and after seeking any necessary legal counsel, the Central Government may, following receipt of the investigation report, instruct the Serious Fraud Investigation Office to file charges against the company, any of its officers or employees who are or have been employed by it, as well as any other person who is directly or indirectly involved in the company's affairs. The Central Government may file an application before the Tribunal for appropriate instructions with regard to disgorgement of such asset, property, or cash and also for holding such asset, property, or cash in reserve in cases where the report indicates that fraud has occurred in a company and that due to such fraud any director, key managerial personnel, other officer of the company, or any other person or entity, has taken undue advantage or benefit, whether in the form of any asset, property, cash, or in any other manner.

POWERS

The director who is not below the position of a joint secretary in the Indian government and has the required knowledge of business frauds assists in the operation of the agency. The SFIO has the sole authority to look into an offence committed in violation of the 2013 Act after receiving a case assignment. In order to aid the SFIO officers in their investigations, it has a Computer Forensic and Data Mining Laboratory (CFDML) since 2013.

Although the SFIO, which is under the corporate affairs ministry, is given arrest authority by the Companies Act of 2013, the provision was first made public in 2017. The majority of the Act's provisions went into effect on April 1, 2014. The guidelines governing arrests in connection with SFIO investigations were announced by the ministry and went into force on August 24, 2017. If they think a person is guilty of any offence related to the case being investigated, an officer not below the rank of assistant director level personnel at the SFIO have the authority to make an arrest. It is important to document in writing why was someone arrested and no arrest can be made without fulfilling this mandatory provision. For all decisions concerning arrests, the director of the SFIO would be the appropriate authority.

Only "with prior written approval of the central government" is the officer of the SFIO who is not

below the rank of assistant director, authorized to make an arrest in relation to a government or foreign company that is under investigation. Additionally, such an arrest must be reported to the managing director or the official in charge of the government company's activities. The officer making the arrest should inform the secretary of the administrative ministry concerned if the individual being detained is the managing director or person in charge of a government company. Every arrest made pursuant to the Companies Act is subject to the arrest provisions of the Code of Criminal Procedure, 1973 (2 of 1974). The authority is constrained because only the directors, additional directors, and assistant directors are permitted to make arrests while a "serious fraud" offence is being investigated. They must have a solid suspicion that a crime was committed in accordance with Section 212 of the 2013 Act, and the officer making arrest must write down the reasons for the arrest.

An inspector appointed to investigate a company's affairs has got wide powers to investigate other body corporates as well including the subsidiary companies and holding companies. He can even make investigations concerning the managing directors, directors, or employees, if he believes that it is relevant to the company's affairs. The Central Government must approve this investigation, and the inspector must make sure that the report on the affairs of these bodies or their managing directors or managers discloses cogent and relevant findings which are relevant to the company's investigation.

“In an investigation, if an inspector suspects the destruction, mutilation, alteration, falsification, or secretion of a company's books and papers, they may enter the location and seize them, allowing the company to extract copies for investigation purposes. The inspector must keep the seized materials in custody until the investigation concludes, then return them to the company or managing director. The inspector may take copies or place identification marks on the materials before returning them. The Code of Criminal Procedure, 1973 (2 of 1974) applies to all searches or seizures.”⁵

CONCLUSION AND SUGGESTIONS

The functions of the Serious Fraud Investigation Office established in India is somewhat similar

⁵ The Companies Act, 2013, § 220, No. 18, Acts of Parliament, 2013 (India)

to the Serious Fraud Office of the United Kingdom. However, the UK's SFO has a wider and more potent role than the Indian SFIO. In contrast to the Indian SFIO, which is restricted to the offences mentioned in the Companies Act 2013, the UK's SFO handles both fraud and cases of bribery and corruption. In addition, the SFO director has the authority to choose whether to look into a specific case based on a set of guidelines. The SFO also has a distinctive system for accepting complaints about alleged criminal activity from a variety of sources, including witnesses, victims, businesses (self-reporting), media outlets, and other law enforcement organizations. These characteristics are not present in the Indian SFIO, which can investigate only the cases handed to it by the central government. The SFIO cannot do anything until and unless it is assigned a case.

Corporate offences involve a lot of money of the country and the time it is brought to the notice of the Central Government, it is often late. So, the need of the hour is that the restriction that is imposed on the mode of assignment of matters to the SFIO should be relaxed to include other stakeholders who may timely report the matter to it. The SFIO is burdened with a difficult and challenging responsibility: combatting corporate fraud. While there is no proof that the SFIO's performance has been jeopardized thus far, there is a risk that it will be abused. Since corporate matters involves considerable amount of money and also the international reputation of the country, it is critical to investigate the SFIO's reliance on the Central Government, especially given the possibility of Central Government personnel being involved in situations such as the Saradha Chit Fund case, where delays in prosecution might have been caused by dishonest motives. This calls into question transparency and accountability. Also, there are circumstances where the frauds may be uncovered in their primary stages and the culprits may be held liable before they abscond. The SFIO should be given the authority to conduct investigations so that it can take on cases and do so without undue interference from the Central Government. There should be an Independent Ombudsman established within the SFIO to manage the prosecution process with some oversight from the Central Government. The SFIO should be empowered to launch its own investigations.

With the growing economy and growth of businesses, the number of corporate frauds is destined to rise and until and unless the SFIO is not given some independent power of launching investigations on its own, the purpose will not be fulfilled. The central government cannot take into consideration all the matters on its own and therefore other stakeholders must be included in the provision so that the corporate frauds can be timely addressed. The working and the overall

strength of the SFIO needs to be improved in order tackle the corporate frauds that will occur with the economic advancement of India.