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# Role of Special Courts under Companies Act, 2013

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## ABSTRACT

*A constant delay in the trials and disposal of the cases have affected the interest of many corporates and the parties related to the companies. Scams happening all around the country and their increasing number have raised many questions which were not answered even in the higher courts due to pendency of so many corporate cases before the tribunal. The enactment of the Companies Act, 2013 (or the 'Act') was one of India's most important and significant legal reforms in the recent past to bring the Indian company law into line with worldwide norms. The present paper deals with the provisions which have been incorporated in the Companies Act, 2013, for the establishment of Special Courts as they are of great significance which leads to the speedy trial of all the offences mentioned under the Act and will also help in the good governance of the Company. It may be noted here that the Special courts are being established for stricter compliance of the company laws and for the benefit of the stakeholders. Special courts were set up by the government so as to induce the companies to comply with the various provisions of the new Companies Act. The constitution of Special courts as judicial authority and National Company Law Tribunal (NCLT) as quasi-judicial authority are the key changes brought in the corporate regime of our country.*

## I. INTRODUCTION

The concept of Special courts is not a new one and there have been various enactments for special criminal courts. The first case that challenged the constitutional validity of special courts was *State of West Bengal v Anwar Ali*<sup>2</sup> in which they were declared unconstitutional but later in the case of *Kathi Raning v State of Saurashtra*<sup>3</sup> the trial by special courts was held to be constitutional.

Ministry of Corporate Affairs constituted the Company Law Committee under the chairmanship of secretary, MCA on 4<sup>th</sup> June, 2015. The committee made recommendations on

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<sup>2</sup> AIR 1952 SC 75

<sup>3</sup> AIR 1952 SC 123

the early establishment of the Special Courts. The Committee took into consideration that the Special courts would result in faster prosecution of defaulting companies. It was also considered that whether Special courts could be established at the sub-ordinate level, in addition to Sessions Judge or Additional Sessions Judge.

The Committee also observed that Section 439(2) does not include the provision for complaints to be filed by the person who is also a member of the company without any share capital. Therefore it recommended to insert the words 'or members' after the term 'shareholder'. The committee further recommended that the power of Special Courts should not be limited to the adjudication of offences punishable with two years or more only and a consequential change ought to be made.

## II. DE- CLOGGING SPECIAL COURTS

The report of the Committee to review offences under the Companies Act, 2013 was constituted by the Government of India on 13<sup>th</sup> July, 2018 to review the offences under the Act and to make recommendations so as to strengthen the existing corporate governance mechanism. A detailed study was made by the committee and the report was presented on 14<sup>th</sup> August, 2018 pursuant to which the corporate ministry has promulgated Companies (Amendment) Act, 2018.

The amendment has now withdrawn the clause whereby the permission of the Special Court was necessary for compounding of the offences punishable with fine or imprisonment or with both thereby increasing the pendency of cases before the special courts constituted under the Act. NCLAT in its judgement in *Cinepolis India Pvt. Ltd. V. ROC*<sup>4</sup> held that the prior approval of the Special Court before compounding of offences by NCLT is not required.

Section 435 of the Act lays down that the Central Government may by notification can establish as many Special Courts as may be necessary. In addition to this, the newly introduced Section 447 of the Act defines 'fraud' in relation to affairs of the company and prescribes stricter penal provisions for indulging in any sort of fraudulent activities.

Section 436(2) of the Act provides that a Special Court may also try an offence other than an offence under the Act whereby the accused may be charged at the same trial in accordance with the Criminal Procedure Code 1973 (in short ' Cr PC). Thus, not only the trial of all offences under the Companies Act, 2013, but also those offences under other Acts can be clubbed for trial of which the Special Court accuses the offender at the time of trial. A research of the provisions of sections 435, 436 and 437 of the Act makes it clear that in criminal instances the

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<sup>4</sup> CA(AT) No. 137 of 2017

Special Judge will exercise original jurisdiction and may also exercise jurisdictions comparable to those exercised by the Magistrate under the Criminal Procedure Code.

Although it is too early to say that a straightforward dissection of the appropriate regulations of the Act relating to the trial of offences indicates that, like the Central Bureau of Investigation ('CBI'), which investigates corrupt practices and charges of corruption by government authorities listed under the Prevention of Corruption Act, 1988 and subsequent trials of perpetrators are conducted by special CBI courts, with the passage of time, the Special Courts established under the Companies Act, 2013 will also assume enormous importance and are likely to assist in the speedy delivery of justice system by prosecuting commercial offenders.

*There comes a question in our minds- Can a corporate entity be imprisoned and how much fines can be imposed?*

This issue is highly contentious as the Supreme Court in *Velliappa Textiles Ltd.*<sup>5</sup> has held that since a corporate entity is not a natural person, it cannot be imprisoned. Where the punishment is "imprisonment and fine", the court cannot award only "fine" as punishment and as such the offending corporate body cannot be given any punishment., howsoever, the offence may be grave , because that discretion is not vested in the court. However, in the case of *Standard Chartered Bank v Directorate of Enforcement*<sup>6</sup> the Supreme Court has reversed the order and held that corporates having committed grave offences cannot escape punishment and the court has to fill the gap/ omission left in the law.

As per Section 446A<sup>7</sup>, while deciding the amount of fine or imprisonment, the court or the special court, shall consider-

- Size of the company,
- Nature of the business carried on by the company,
- Injury to the public interest,
- Nature of default and repetition of default.

### III. FRAUD

Before we begin to analyse the provisions relating to the establishment of the Special Courts and the 'cognizable, and 'non-cognizable' offences under the Act, it is essential to look at section 447 of the Act, which has broadened the scope of 'fraud' and clarifies that fraud in

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<sup>5</sup> (2003) 46 SCL 808

<sup>6</sup> (2005) 59 SCL 217

<sup>7</sup> Inserted vide Companies (Amendment) Act,2017

relation to the business of a company or any corporate entity includes any act, omission or concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with the intention of deceiving or gaining undue advantage from, or harming the interests of the company or its shareholders or its creditors or any other person. Any such individual, including the company, found guilty of fraud, shall be punished with a rigorous penalty of up to three times the amount of fraud and a minimum imprisonment of term ranging between six months to ten years. In order to dissuade fraudulent acts influencing the “public interest” the Act clarifies that the minimum imprisonment term is not less than three years as opposed to the minimum 6-month period in other cases. Also, the said section clarifies what is ‘wrongful gain’ and ‘wrongful loss’.

#### ***Instances Of Fraud Provided In The Act-***

There are certain instances, where the acts amount to fraud and therefore the person responsible for such act would be liable to fine and punishment. Some such instances provided under the act are-

1. Incorporation of a Company with incorrect or false information or suppression of any material fact [Section 7(5) and (6)]
2. Misleading or untrue statements in respect of Prospectus [Section 34]
3. Fraudulently inducing any person to invest money [Section 36]
4. Personation for acquisition of securities [Section 38]
5. Acceptance of deposits with intent to defraud depositors [Section 75]
6. Where Auditor of the Company acts in a fraudulent manner [ Section 147(5)]
7. Affairs of the Company are carried on for unlawful purpose with an intent to defraud shareholders, creditors or any other person [Section 213]
8. Furnishing any false statement, mutilation, destruction of documents during the investigation or inquiry. [Section 229]
9. Furnishing false statement and giving false evidence [ Section 448 and 449]

#### **IV. COMPOSITION OF SPECIAL COURT**

Section 435 of the Act stipulates that a Special Court shall consist of a single Judge appointed by the Central Government with the approval of the Chief Justice of the High Court in whose jurisdiction the Judge to be appointed shall function and states that an individual shall not be eligible for appointment as Judge of a Special Court unless he, immediately before such

appointment, was holding the office of a Sessions Judge or an Additional Sessions Judge. Thus, it becomes quite apparent that the central government is very serious about punishing corporate offenders and the judge who will try these corporate offences being not less than the rank of a Sessions Judge or Additional Sessions Judge shall have adequate experience, knowledge and sensitivity to attempt such severe offences and bring justice.

## **V. JURISDICTION AND POWERS**

Jurisdiction and powers of the Special courts may be traced in Section 436 of the Act which provides those offences triable by the Special courts.

Section 436 of the Act provides that, notwithstanding anything contained in the Code of Criminal Procedure, 1973 (hereinafter referred to as 'Cr PC '), all offences under the Act shall be liable to be tried only by the Special Court established for the area in which the company's registered office is situated in relation to the offence committed or where there are more Special Courts than one for such area then by one of them as may be specified in this behalf by the concerned High Court. Regarding the detention of an accused person.

Section 436(1)(b) of the Act provides that where a person accused or suspected of committing an offence under the Act is forwarded to a Magistrate under Section 167(2A)(2) of the Cr PC, then such Magistrate may authorize that person to be detained in such custody as he considers fit for a period not exceeding fifteen days in whole, where that Magistrate is Judicial Magistrate and seven days in the whole, where that Magistrate is an Executive Magistrate. Where that Magistrate believes that the detention of that individual is unnecessary at or before the expiry of that detention period, that Magistrate shall order that individual to be sent to the Special Court. Since the Act stipulates the imminent arrest of accused corporate officers, it would hopefully discourage fraudulent commercial activities.

Section 436(1)(c) of the Act provides that the Special Court may exercise, in relation to a person referred to it pursuant to clause (b) of Section 436(1) of the Act, the same power as that exercised by a Magistrate with jurisdiction to try a case pursuant to Section 167 of Cr PC in relation to a accused person who has been referred to him pursuant to that section. Also, Special court may, at the perusal of police report of facts constituting the offence under the Act or on a complaint in this behalf, take cognizance of that offence without committing the accused for trial.

Section 436(2) provides that while trying an offence under this Act, special court may also try any offence other than provided in this act with which accused is charged at the same trial under Cr PC. This widens the scope and jurisdiction of the trial at Special Court which is a

welcome move.

In the case of **Sunil Mandwani v State of Madhya Pradesh**<sup>8</sup>, the court held that criminal proceedings against the applicants have not been initiated for any offence punishable under the provisions of the Act, and therefore, in the absence of any offence punishable under Companies Act, the Special Court has no jurisdiction to try a case punishable under the Indian Penal Code. The territorial jurisdiction to try the case rests with the Court of Indore for the offences punishable under Section 120-B, 467, 420, 468 and 471 of IPC. The petition for revision was thus, rejected.

#### ***Power to try Offence Summarily-***

Section 436(3) of the Act provides that, notwithstanding anything contained in Cr PC, the Special Court may, if it considers fit, summarily try any offense under this Act punishable by imprisonment for a term not exceeding three years, provided that in case of any conviction in Summary Trial, no sentence of imprisonment for a term more than one year is passed.

Further, it is provided that, at the beginning of a summary trial or during a summary trial, it appears to the Special Court that the nature of case is such that the sentence of imprisonment might exceed one year threshold, or it feels that it is unwanted to summarise the case then the court shall record an order to that effect and then recall any witness who might have been examined and thus proceed to hear or rehear the trial in same way as a regular trial.

#### ***Power to act as a Court of Session-***

Section 438 of the Act provides that the Special court shall proceed in the same manner as a court of session under Cr PC and it shall be deemed to be a Court of session or a Judicial Magistrate of First Class or the Court of Metropolitan Magistrate. The person who will conduct the prosecution shall be deemed to be Public Prosecutor.

#### ***Power to Grant Relief***

This article would be incomplete if we do not mention the power of the special court to grant relief in certain cases which is mentioned in Section 463 of this Act. Section 463(1) states that if it appears to the court, in any proceeding for default, negligence, breach of duty, breach of trust or misfeasance against any officer of a company, that he has acted honestly and reasonably, the Court may relieve him, either wholly or partly, from his liability on such term, as it may deem fit.

Proviso to this section stipulates that in a criminal proceeding under this sub-section, the Court

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<sup>8</sup> 2019 SCC online MP 1248

shall not have any power to grant relief from any civil liability which might be attached to an officer in respect of such default, negligence, breach of duty, breach of trust or misfeasance.

The court shall not grant any relief to any officer unless it has required the Registrar and such other person( by notice served in the manner specified by it) to show cause notice that why such relief should not be granted.

### ***Appeal and Revision-***

The High Court shall hear the appeals filed against all the orders of the special court within whose local jurisdiction that special court is functioning. Also the High Court may exercise all the powers conferred by the Cr PC under chapters XXIX and XXX as far as applicable.

It is expected that with the full functioning of Special Courts under this Act, the labyrinth of cases, which were otherwise handled by a Magistrate, will not come in way to speedier justice in cases of corporate fraud or corporate misconduct.

## **VI. COGNIZANCE OF OFFENCES**

Section 439 of the Act provides that notwithstanding anything under Cr PC, every offence shall be deemed to be a non-cognizable offence except those offences referred to in section 212(6) of this Act. The special Curt shall take cognizance of any offence committed by any Company or any Officer of that company only on the complaint made in writing by the

- Registrar
- A shareholder or a member of the company, or
- A person authorized by Central Government in this behalf.

Therefore, a single shareholder can invoke the legal regulations and initiate the Special Court proceedings. The law enables authorized SEBI representatives to file cases related to offences including issue and transfer of securities and non-payment of dividends. In this section, company cannot prosecute any of its officers.

Although section 439 talks about non-cognizable offenses, ,an analysis of section 212(6) of the Act becomes essential for knowing the type of offences which are ‘cognizable’ notwithstanding anything contained otherwise in the Cr PC as it states that no person who is accused of any (offence under section 447)<sup>9</sup> of the Act shall be released on bail or on his own bond, unless the Public Prosecutor has been given an opportunity to oppose the application of such release and where the Public Prosecutor opposes such application but the Court is satisfied that there are

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<sup>9</sup> Subs. By Act 21 of 2015

reasonable grounds for believing that the accused is not guilty of such offence and that the accused is not likely to commit any offence while on bail, the Court may order the accused to be released on bail. Nevertheless, if the Special Court directs, a person below age of sixteen years or a sick or infirm or a woman may be released on bail. Special Court shall not take the cognizance of any offence which is referred to in Section 212(6) of the Act, except on a complaint made by-

- the Director, SFIO, in writing or
- any officer of Central Government authorized by any general or special order in writing in that behalf.

## VII. ROLE OF SERIOUS FRAUD INVESTIGATION OFFICE

Serious Fraud Investigation Office (SFIO) which was established by the Central Government vide resolution number 45011/16/2003 – Admin- I dated 2 July, 2003 has already been doing a great job in investigating the frauds committed by companies. The SFIO came into effect from 21 July 2015.<sup>10</sup>

The newly introduced Section 211 of the Act gave a legal effect to SFIO in the Act itself. The Central Government is authorized to set up SFIO. Section 212(1) of the Act provides that where the Central Government thinks that it is necessary to investigate into affairs of the company, it may assign that investigation to the SFIO. The Central Government may by order make an assignment under the following circumstances-

- a) on receipt of report of the Registrar or inspector under section 208,
- b) on the intimation of special resolution passed by a company that the affairs of such company are required to be investigated,
- c) in the public interest
- d) on the request from Central or State Government Departments.

It is essential to note here that the SFIO cannot undertake the investigation *suo motu*, i.e. a special reference is needed. In the case of Parmeshwar Das Agarwal v Additional Director (Investigation)<sup>11</sup>, it was held that an investigation by SFIO ought to be on the basis of opinion of the Central Government that it was necessary to investigate into affairs of the company.

SFIO can now get the offenders prosecuted at the Special Court as 'Fraud' is now defined in

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<sup>10</sup> Vide Notification SO 2005(E) [F.No.A – 35011/09/20111- ADMIN III]

<sup>11</sup> [2016] 75 taxmann.com 261 (Bombay)

the Act. The SFIO upon the completion of the investigation assigned to it shall submit a report to the Central Government within such period as may be specified. If directed by the Central Government, an interim report shall also be submitted.

The Central Government may also direct the SFIO to take steps for the prosecution of the company and its officers or employees( past or present) or any other person directly or indirectly involved in the affairs of the company. The investigation report filed with the special court for framing charges shall be deemed to be a report filed by police officers under 173 of Cr PC, 1973.

### **VIII. ROLE OF SPECIAL COURTS UNDER IBC, 2016**

Special courts have been given wide jurisdictional powers under the Insolvency and Bankruptcy Code, 2016. Section 236 of the IBC provides that all the offences under the said code shall be tried by the Special Courts established under the Companies Act, 2013. The court shall take cognizance of the offence only after the complaint is made in writing by the Board, Central Government or any person authorised on this behalf. In the offences relating to Insolvency and Bankruptcy also, the Special courts shall be deemed to be the Court of Session and any person who shall be conducting the prosecution be deemed to be a Public Prosecutor.

### **IX. ADARSH CREDIT CO-OPERATIVE SOCIETY SCAM- A CASE STUDY**

Adarsh Credit Co-operative Society Ltd was a reputed multi state credit Co-op. society which started its operations in 1999 and is based in Ahmedabad. Mukesh Modi is the founder and Rahul Modi is the Managing Director who were alleged to have siphoned off around rupees 800 crore of around 20 lakh depositors by running Ponzi Schemes.<sup>12</sup> It was observed that the deposits which were collected from the members of the Co-operative Society were being used for the benefit of the family members of Mukesh Modi, thereby violating the principles of co-operative societies.

Central Government had directed the investigation into the affairs of Adarsh group of companies and LLPs to Serious Fraud Investigation Office(SFIO) on 26/06/2018. Pursuant to the investigation, the arrest order were made for three accused persons namely, Rahul Modi, Mukesh Modi and Vivek Harivyasi and they were arrested o 10/12/2018. The accused were produced before the **Special Court** and after the court was satisfied that further investigation is required, the accused persons were remanded to police custody till 14/12/2018.

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<sup>12</sup> A Ponzi Scheme is a form of fraud which lures the investor and pays them high rates with little risk.

A Writ Petition<sup>13</sup> was filed by the accused on 18/12/2018 under Article 226 and 227 of the Constitution of India read with 482 of Cr PC in the High Court of Delhi and later the court granted bail to both Rahul Modi and Mukesh Modi. The extension proposal was filed by SFIO and was accepted by the Central Government and the extension was granted up to 30/06/2019 to examine whether the High Court was competent to grant the bail against whom SFIO had initiated prosecution proceedings for siphoning off over 200 crore rupees.

The Supreme Court asked Modi to satisfy it whether H.C. was a competent court to grant them bail when the prosecution was initiated in Gurugram, Haryana. Tushar Mehta, Solicitor General, appearing for SFIO said that the High Court does not have the territorial jurisdiction to set aside the order of Gurugram Special Court. Supreme Court directed the petitioners to surrender and the Special Court, Gurugram was directed to consider the case on merits.

## **X. CONCLUSION**

From the above discussion and the legal provisions, it is clear that the Special Courts would function in addition to the NCLT and the professionals who are associated with the corporate field would be benefitted if they keep themselves abreast with all the amendments in the companies Act and guide the management of the companies to comply with all the requirements in the new Act. As we all know now that the new changes in the act now involves the offences relating to the formation of the companies, the casual approach taken by the professionals of lending their names in this regard should be totally avoided. The companies cannot become reckless or disregard the requirements of the stricter penal provisions which are introduced in the new Act. If they continue to do so, it will be at their risk and peril.

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<sup>13</sup> Writ Petition (Criminal) Nos 3842 & 3843 of 2018

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