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# Not a perfect formula

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In the past, Indian laws and courts used to be quite cagey about consent settlement. A new chapter has, however, been incorporated in the Code of Criminal Procedure, 1973 in 2006 to facilitate some sort of consent settlement of most kinds of offences, which attract imprisonment of up to seven years. The advantages of this kind of settlement are many in the Indian context. In short, it achieves the public good that there be an end of litigation, Expedit reipublicae ut sit finis litium.

But, often the mechanism was misused by a few to prolong the proceeding indefinitely by making repeated applications, offering successively better terms of settlement for the same default. The new framework of consent settlement of defaults in the securities market ushers in some good practices, bringing to an end many ills of the past, but has made it unworkable.

The earlier framework allowed settlement of all kinds of defaults as long as the terms of settlement were appropriate. The new framework debars settlement of serious FUTP (Fraudulent and Unfair Trade Practises) defaults, ICDR defaults which materially affect the rights of investors and MF (mutual fund) defaults,

which have resulted in substantial loss to the unit holders, among others. The words ‘serious’, ‘materially’ and ‘substantial’ being subjective, legitimatise discretion of the Securities and Exchange Board of India (Sebi). The HPAC (High Power Advisory Committee)/panel of WTMs (whole-time members) have, however, been granted discretion to settle any default irrespective of its kind and gravity. Thus, the new framework practically allows settlement of all kinds of defaults, but requires invocation of discretion.

Sebi will use discretion initially to deny consent in serious cases while the HPAC/panel of WTMs will use discretion subsequently to allow consent in those very cases. The delinquent would have no clue whether a particular default is consentable. And, whether a particular default is consentable would be contestable.

The new framework prescribes a formula to arrive at the terms of settlement. This robs the consent mechanism of its soul. A formula, howsoever, robust and comprehensive it be, can’t capture all possible factors having a bearing on the terms of settlement. For example, it can’t capture the strength of evidence and consequently the probability of conviction. Take the case of a default, which warrants a consent settlement of Rs 1 crore according to the formula. If, however, the evidence available is such that the probability of conviction is 0.1, the delinquent would never settle the default for Rs 1 crore. It may not mind settling it for Rs 10 lakh if the strength of evidence is factored in. This explains why a few defaults were not settled earlier under consent even though the delinquents offered handsome amounts, but it was completely exonerated subsequently on adjudication on merits. Its unintended consequence is that only the defaults with substantial evidence would be settled under consent while the defaults with inadequate evidence would be adjudicated on merits.

A formula-driven approach delivers if the settlement is in monetary terms only. However, the framework rightly allows, wherever necessary, suitable directives under the consent order. These directives, such as cancellation of registration, debarment from market, compensation to investors and disgorgement of unlawful gains could often be more effective and equitable. But, since it would be difficult to establish equivalence between monetary terms and such directives, the new framework would encourage settlement of defaults mostly in monetary terms, which may not always achieve the objectives of enforcement actions.

A formula has laudable objectives to ensure that the consent terms are commensurate with the default and uniform for similar defaults. However, since it can’t factor in all possible factors, it would occasionally overestimate the terms of

settlement and deny settlement in an otherwise deserving case and vice versa. If no formula is used in adjudication where there is application of mind by one person only, it is not necessary to use a formula in consent settlement, which passes through three committees and application of mind by at least nine persons, including a justice and two whole-time members.

Ideally, any default, irrespective of its nature and gravity, should be settled through consent, subject, however, to the condition that the settlement terms are appropriate to the alleged default, that is, at least the same or equivalent outcomes, as would have been obtained if the proceedings were adjudicated on merits, are achieved. For example, if a default warrants a penalty of Rs 1 lakh on adjudication, it should be settled under consent only if the delinquent either admits the guilt and pays Rs 1 lakh, or does not admit or deny the guilt and pays Rs 2 lakh. If the terms are not appropriate, the consent application should be rejected as happens today in about 40 per cent of the cases. While the authorities should have no discretion as to which defaults can be settled under consent, they should have full discretion to determine the terms of settlement keeping in view all the relevant factors.

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