

Misrepresentation in Prospectus: An Analysis of Civil and Criminal Liabilities

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A prospectus is a legal document that provides detailed information about a financial security or investment opportunity that is being offered for sale to the public. It typically includes information such as the terms and conditions of the offering, the risks associated with the investment, the financial statements of the issuer, and any other relevant information that potential investors may need to make an informed decision about whether or not to invest.

Misrepresentation in a prospectus refers to the act of making a false statement, omitting material information, or providing misleading information in a prospectus. This is a serious offense because a prospectus is a legal document that investors rely on to make informed decisions about whether or not to invest in a security. If a company or its directors are found to have made a misrepresentation in a prospectus, they may face both civil and criminal liability.

Under the Indian Companies Act, 2013, any person who is responsible for the misrepresentation in a prospectus can be held liable. This includes the company, its directors, and any other person who has authorized the issue of the prospectus. Civil liability may result in a lawsuit being brought against the company or its directors by investors who suffered a loss as a result of the misrepresentation. The court may order the company to pay damages to the investors to compensate them for their losses.

In addition to civil liability, there may also be criminal liability. The Indian Companies Act, 2013 provides for criminal penalties for anyone who makes a false statement or misrepresentation in a prospectus. The penalties may include imprisonment and/or a fine. The severity of the penalty will depend on the nature and extent of the misrepresentation.

The prospectus is an important document in the securities market as it provides information to potential investors about the company, its operations, financial position, and the securities

being offered for sale. It allows investors to make informed decisions about whether or not to invest in a particular security. The prospectus also helps to ensure transparency and fairness in the securities market, which is important for investor protection and the overall health of the economy.

Misrepresentation refers to a false statement of fact made by one party to another, which induces the other party to enter into a contract or take some other action. In the context of a prospectus, misrepresentation can occur when the information contained in the document is inaccurate, incomplete, or misleading.

Types of Misrepresentation in Prospectus:

Innocent Misrepresentation: It occurs when a false statement is made by mistake or without any intention to deceive.

Negligent Misrepresentation: It occurs when a false statement is made due to the failure of the company to exercise reasonable care in verifying the accuracy of the information.

Fraudulent Misrepresentation: It occurs when a false statement is made with the intention to deceive or with reckless disregard for the truth.

Factual misrepresentation: This occurs when a prospectus contains inaccurate information, such as incorrect financial statements, false statements about the company's business operations or assets, or other incorrect facts.

Omission of material facts: This happens when a prospectus fails to include important information that would impact an investor's decision to invest, such as a pending lawsuit or regulatory action.

Forward-looking statements: These are statements about future events, such as projections about the company's future financial performance. If these statements are not based on reasonable assumptions or if they turn out to be inaccurate, investors may be misled.

Exaggerated claims: These are statements that overstate the company's potential or the benefits of investing in the company.

Insider trading: This occurs when individuals with inside knowledge of a company's affairs use that knowledge to trade securities in the company before the information becomes public.

It is important for companies and organizations to ensure that their prospectus accurately and completely discloses all relevant information to potential investors to avoid misrepresentations that can result in legal liability.

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Examples of Misrepresentation in Prospectus:

Overstating the company's financial performance by inflating revenue or understating expenses.

Concealing material facts, such as ongoing litigation or regulatory investigations, that could have a significant impact on the company's future prospects.

Making false statements about the company's products or services, such as their safety or effectiveness.

Consequences of Misrepresentation in Prospectus:

Civil Liability: Any person who suffers a loss as a result of misrepresentation in a prospectus can sue the company for damages.

Criminal Liability: The company and its officers can also face criminal charges for making false statements in a prospectus, which can result in fines and imprisonment.

Regulatory Action: The Securities and Exchange Board of India (SEBI) can take action against the company for violating disclosure norms, including imposing fines and banning the company's directors from accessing the capital markets.

Misrepresentation in a prospectus refers to providing false or misleading information to investors in the prospectus. This is a serious offense and can lead to civil and criminal liability for the company and its directors.

Civil Liability for Misrepresentation in Prospectus:

Section 34 of the Indian Companies Act 2013 deals with civil liability for misrepresentation in a prospectus. According to this section, any person who has subscribed to securities or purchased them from the company can sue for damages if the prospectus includes any untrue statement or omits any material fact.

The following persons can also sue for damages under this section:

Any person who has acquired securities with the consent of the company.

Any person who is a legal representative of a person who could have sued for damages if he had been alive.

Under company law, a prospectus is a legal document that provides details about the company and its securities to potential investors. If a prospectus contains any misstatement or omission of material facts, it may result in civil or criminal liability for the company and its officers.

Remedies for Misstatements in Prospectus:

Civil Liability: If a prospectus contains any misstatement or omission of material facts, the investors who have suffered loss or damage as a result of such misstatement can file a civil suit against the company, its directors, and other persons who authorized the issue of the prospectus. The remedies available to the investors in such cases include damages, rescission of the contract, and an injunction against further sales of securities.

Criminal Liability: If a prospectus contains any false statement or misrepresentation of material facts, the company and its officers may be held criminally liable under the provisions of the Companies Act. The penalties for such offenses may include fines, imprisonment, or both.

Remedies for Criminal Liability:

Criminal Proceedings: The Securities and Exchange Board of India (SEBI) can initiate criminal proceedings against the company and its officers for any misstatement or false statement made in the prospectus. The proceedings can result in imprisonment, fines, or both.

Imposition of Penalty: SEBI may also impose penalties on the company and its officers for any violation of the securities laws, including the making of false statements or misrepresentations in the prospectus.

Debarment from Securities Market: SEBI has the power to debar the company and its officers from the securities market if they are found to have violated the securities laws. This can result in the company and its officers being prevented from raising funds from the capital markets.

In conclusion, misrepresentation in a prospectus is a serious offense that can lead to civil and criminal liability for the company and its directors. Investors who have been misled by false or misleading statements in a prospectus can sue for damages under Section 34 of the Indian Companies Act 2013.

In India, the Companies Act of 2013 imposes both civil and criminal liability for misrepresentation in a prospectus. Civil liability

refers to the legal responsibility for damages or losses incurred by an aggrieved party, while criminal liability refers to the legal responsibility for committing a crime.

Section 447 of the Companies Act, 2013 provides for punishment for fraud, which includes any act of deception or misrepresentation with the intent to deceive, whether by omission or commission, committed by a person or company in the course of its business. The section prescribes a minimum imprisonment of six months, which may extend to ten years, and a fine of at least the amount involved in the fraud or up to three times the amount of the fraud, whichever is higher.

In cases of misrepresentation in a prospectus, if the misrepresentation is found to be fraudulent, the person or company responsible may face criminal liability under Section 447 of the Companies Act, 2013. The consequences may include imprisonment and hefty fines.

On the other hand, civil liability arises from a breach of contract or a duty of care owed to the aggrieved party. In the context of misrepresentation in a prospectus, civil liability may arise if a person or company makes a false statement or omits material information from the prospectus, causing loss or damage to investors who relied on that information. In such cases, the aggrieved party may sue the person or company responsible for damages.

One notable case in this regard is the Satyam Computer Services scam, where the company's founder and chairman, Ramalinga Raju, was found guilty of financial fraud, including misrepresentation in the company's prospectus. Raju was sentenced to seven years in prison and was ordered to pay a fine of Rs. 5.5 crores. The case highlighted the seriousness of misrepresentation in a prospectus and the legal consequences that may follow.

Section 35 of the Indian Companies Act 2013 imposes duties on directors to ensure that the information contained in a prospectus is accurate and not misleading. If a director makes a misrepresentation in a prospectus, he or she may be held civilly and criminally liable for any losses suffered by investors as a result.

Civil Liability: If a director is found to have made a misrepresentation in a prospectus, he or she may be sued by investors who suffered losses as a result. Under Section 35, the director may be required to pay damages to compensate the investors for their losses.

Criminal Liability: If the misrepresentation in the prospectus is found to be fraudulent or reckless, the director may face

criminal charges under Section 447 of the Companies Act 2013. If convicted, the director may be sentenced to imprisonment for a term ranging from six months to ten years, and may also be fined.

Exceptions to Director's Liability: There are certain exceptions to director's liability for misrepresentation in prospectus, which are as follows:

The director had reasonable grounds to believe that the statement was true.

The statement was immaterial or irrelevant to the prospectus.

The director withdrew his or her consent to the prospectus before it was issued, and gave reasonable public notice of such withdrawal.

The prospectus was issued without his or her knowledge or consent, and on becoming aware of it, he or she immediately withdrew his or her consent and gave reasonable public notice of such withdrawal.

Case Laws: Some notable cases related to misrepresentation in prospectus and director's liability in India are:

Sahara India Real Estate Corp. Ltd. and Ors. v. Securities and Exchange Board of India and Anr. (2012): The Supreme Court held that the directors of a company are responsible for ensuring the accuracy of the information contained in the prospectus, and that they cannot escape liability merely by delegating the task to others.

Satyam Computers Services Ltd. (2009): The Satyam scandal involved the largest corporate fraud in Indian history. The directors of the company were held liable for making false statements in the company's prospectus, and were also charged with criminal offenses.

These cases demonstrate the importance of accurate disclosure in prospectuses and the potential consequences for directors who fail to ensure the accuracy of the information contained therein.

In the Indian Companies Act 2013, misrepresentation in a prospectus can lead to both civil and criminal liability. Civil liability may result in the company being sued for damages by investors who suffered losses due to the misrepresentation. Criminal liability may result in fines and imprisonment for the company's directors and officers who were involved in the misrepresentation.

Compliance with regulations is crucial for companies to avoid liability and maintain trust with investors. It is important for companies to ensure that all information disclosed in the prospectus is accurate, complete, and not misleading. Companies

should also review and update their prospectus disclosures regularly to reflect any material changes in the business or industry.

To improve prospectus disclosures, companies should focus on providing clear and concise information that is easy to understand. They should also disclose all relevant information, even if it may be unfavorable or negative. This includes information about risks and uncertainties associated with the business, as well as any legal or regulatory issues.

Further research could be done to explore the effectiveness of current regulations and enforcement mechanisms in preventing misrepresentation in prospectuses. It would also be useful to study the impact of improved prospectus disclosures on investor confidence and market efficiency.

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