



Companies Bill, 2012

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More on Companies Bill 2012

There are lots of materials and articles on the Companies Bill 2012 here:

<http://india-financing.com/component/content/article/281.html>



Overview and quick comments

Structure of the Bill

- Existing Act had some 658 sections and 14 Schedules
- New Bill has 470 sections and 7 schedules
- However, don't be misled to believe that the Bill is any shorter or simpler
 - Huge amount of law has been moved into the rules
 - There are 416 occurrences of the word “prescribed”
 - This means a tremendous body of rule making
 - Several sections have been consolidated into single section
- In fact, there are lots of new provisions, new restrictions and approvals to be sought
 - 74 occurrences of “special resolution”
 - 15 occurrences of “approval of the Central Government”

However, opens lots of avenues for professionals

- NCLT and NCLAT both open for chartered accountants, cost accountants and company secretaries
- Registered valuers
 - Prescribed qualifications to be laid
- Company Liquidator
 - Panel to be maintained
- Conciliation Panel
 - Experts to be listed
- Panel of independent directors



Several new concepts

- One person company
- Dormant company
- Class action
- Freeze action
- Mandatory corporate social responsibility
- Mandatory retirement of auditors
- Mandatory retirement of independent auditors
- Pecuniary relationships completely ruled out in case of independent directors
- A whole new set of provisions for private placements
- National Financial Reporting Authority
- Non-judicial approval of mergers
- Moratorium powers in case of sick companies

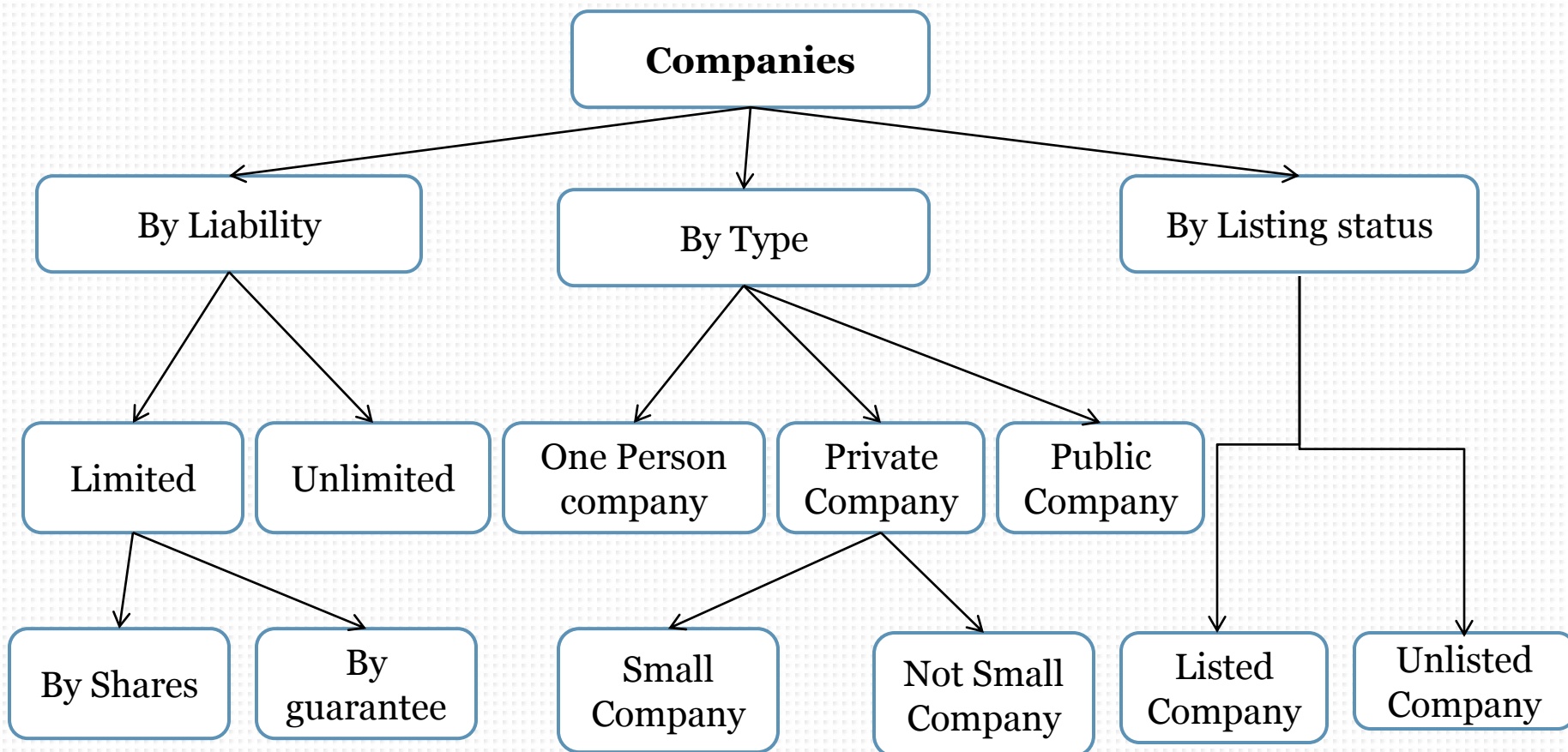
Troublesome provisions

- Independent directors not to have any pecuniary relation at all
 - As the provision travels back in time, existing independent directorships to be affected
- Civil liabilities for auditors
 - Exposing auditors to massive claims
- Exemptions for private companies thin and meagre
 - Of course, one will need to see the notifications



Preliminary

Types of Companies





Types of Companies

- One person company – one member
- Private company – upto 200 members
 - **Small companies**
 - Paid up capital Rs 50 lacs; turnover Rs 2 crores
 - In our view, both these conditions need to be complied with
 - Should not be a holding co or subsidiary co
 - **Other private companies**
 - Not being a small companies
- Public companies
- Limited and unlimited companies
- Conversion from public to private companies will need sanction of NCLT

Holding and Subsidiary Companies

- Change in definition – not sure whether this was done consciously or otherwise
 - The trigger is now based on more than 50% of total share capital, rather than 50% of voting capital
 - In other words, an entity may hold substantial part of equity, and still not be a holding company
 - Note accounting consolidation is still based on equity shares or voting shares.
- Another important point is that the law now seeks to empower the CG to limit the no of layers of subsidiary companies in certain class of companies.
 - What could be the intent behind this – not clear

Promoters

- Persons in accordance with whose directions the board of directors is accustomed to act is also included in the definition of promoters
- This increases the gap between the definition under Securities laws and Companies Act

Public Financial Institutions

- All existing PFIs will be included in the new definition
- However, the power to notify new institutions is only limited to entities in which the CG or State govts hold 51% capital
- In other words, infrastructure finance companies will cease to be entitled to the benefit

Memorandum and Articles

- Articles May contain entrenchment provisions
- Entrenched provisions may be altered
 - In case of private companies, by consent of all members
 - In case of public companies, by SR
- Alteration of the MoA
 - SR to be needed for any alteration
 - Since authorised capital is also a part of the contents of the MoA, SR is needed for that as well
 - This is unreasonable, as increase in authorised capital may be required
 - In case of change of objects for companies which have raised public money by prospectus, lying unutilised, change of objects will have to be supported by an exit option



Accounting and auditing related provisions



Audit and Accounting Standards

- Auditing standards to be prescribed by CG in consultation with ICAI
- Financial statements defined
 - Cashflow statement becomes mandatory
- Statement of changes in equity

Accounting Terms

- **Financial year**
 - Mandatorily 31st March
 - Existing companies to align within 2 years
 - NCLT given powers to exempt in case of entities which are holding cos or subsidiary companies of foreign companies
- **Free reserves**
 - Defined to include such reserves as available for distribution
 - Credit balance in P/l a/c is not a reserve
 - Definition already tuned to requirements of IFRS on fair value accounting

Accounting Terms (contd.)

- **Net worth**

- This definition is dangerous, and perhaps has not been noted. The definition seems to say – only paid up capital, share premium and reserves created out of profit will be treated as net worth.
- Surprisingly, credit balance in P/L account has been left out.
- In other words, companies will be left with no choice but to transfer profits from P/L account to “reservers”

- **Internal audit:**

- To be mandatory for such class of companies as CG may prescribe
 - If mandatory, existing internal auditors, if CA, CWA, can continue
 - Clause 144 prohibits statutory auditors to render internal audit
- Auditor may be CA, CWA or such other professional as the CG may lay down



Auditors

- **Appointment of auditors**
 - Currently, appointment is done every year
 - Under the new scheme, appointment is done once for 5 years
 - Ratification done every year
 - The law is casually confusing between “ratification” and “reappointment” taking these two expressions to mean the same
 - Mandatory retirement after 5 years in case of individual and 10 years in case of firms
 - no auditor/audit firm/ audit firms having common partners, shall take audit for a consecutive term of 5 years after 5 years have been completed
 - Provision applicable to all listed companies, and companies of such class as may be prescribed
 - Lots of questions arise
 - Can auditors be appointed for less than 5 years?
 - Answer seems to be no
 - Can a company reappoint an auditor if the auditor resigned before completing the term of 5 years?
 - The law seems to be using the word “more than one term of five consecutive years”
 - However, first proviso to sub-section (2) seems to put a freeze of 5 years



Auditors (contd.)

▫ **Removal of auditors:**

- For not reappointing the retiring auditor, the law now requires special resolution, rather than ordinary resolution with a special notice
- Not sure was this consciously done or crept out of oversight
- For removal of auditor also, special resolution is sought now, in addition to CG approval

Fraud Reporting

- **Fraud reporting**
 - No, audit is not turning into forensic audit
 - But frauds against the company by any of its officers, or employees, are noticed by the auditor, the auditor shall report the same to the CG, within such time as may be laid by rules



Auditors & Non-audit Services

- **Auditors not to provide non-audit services**
 - Following services not to be provided
 - accounting and book keeping services;
 - internal audit;
 - design and implementation of any financial information system;
 - actuarial services;
 - investment advisory services;
 - investment banking services; 30
 - rendering of outsourced financial services;
 - management services; and
 - any other kind of services as may be prescribed
 - not to the company, holding company, or subsidiary
 - directly or indirectly
 - indirectly includes through relative, connected or associated person, or other entity over which individual has significant influence or control, or whose name or trade mark or brand is used by the individual



Auditors: Civil Liability

- **Civil liability for auditors – auditors, make your pockets deep**
 - important provision for civil liability of auditor – sec 147 (3) says if the auditor is convicted u/s 147 (1) (offence of any of the provisions pertaining to audit), the auditor will be liable to compensate companies, statutory bodies and persons who have suffered loss
 - this will open floodgates of claims against auditors

Accounts and Audit

- **Consolidation** becomes mandatory for all companies
 - Strangely enough, consolidation has been provided for in case of associates and joint ventures
 - In case of associates, there is an equity method of accounting – which is not full scale consolidation
 - In case of JVs – consolidation is required only in case of certain JVs
 - Those that maintain separate books of account
 - In addition, the definition of “associate” as per the Act does not match with the definition as per accounting standards
 - Ideally, law should have provided for the AS to prevail

Accounts and Audit (contd. 1)

- **Recasting of accounts**
 - For the first time, a statutory permission for recasting
 - Two types of recasting – mandatory/ voluntary
 - **Mandatory**
 - Provision, allowing recasting only on application by certain authorities or “any concerned person”
 - But NCLT /court has to come to a finding that there was either a case of fraud or mismanagement
 - That is, there is no recasting of accounts if there was a case of error

Accounts and Audit (contd.2)

▫ Voluntary Recasting

- Highly confused language of sec 131 – this is what it means if we straighten it
 - Directors may prepare revised statements, and the company may make an application to NCLT
 - This pertains to a previous financial year – that is, the one for which accounts have been closed
 - NCLT to consider CG and IT authorities in disposing of the application
 - Application allowed once in a year

Accounts and Audit (contd.3)

- **Filing of annual accounts**
 - Currently, difficulties are faced in filing of annual accounts because they are not adopted by the AGM
 - The new law provides for provisional filing of un-adopted accounts
 - Also mandatory filing even where the AGM is not held



National Financial Reporting Authority

- A new quasi-judicial body comes up – NFRA
 - To oversee compliance of accounting and auditing standards
 - To oversee quality of service of professionals associated with preparation of financial statements
- It is a complete new quasi judicial body – complete with Appellate Authority, having powers of a civil court
- Professional misconduct of chartered accountants also comes under NFRA
 - Does this directly clash with the disciplinary powers of the ICAI?
 - Section says, the powers of NFRA shall exclude the powers of the ICAI to investigate into the same misconduct



Directors



Directors

- Important provision
 - At least one director must be a resident in India – a person who has stayed in India for 182 days in the previous calendar year
 - And for some classes
 - There must be woman director

Managerial personnel

- CEO and CFO defined in the Act
 - CEO defined based on designation, not function
- KMP defined to include CEO, CFO, CS, WTD and other notified designations

Officers in default

- A small innocuous change in sec. 2 (60 (vi) makes a director liable as an officer in default even if he is aware of the contravention, merely by virtue of receiving the proceedings of the meeting.
- That is to say, it is not a good defence for a director to say that he did not participate in the proceedings where an alleged contravention arose.
 - However, curious question is – if the director has not participated in the decision-making, and subsequently became aware of the same, how does he avert it?
 - And therefore, how does he save himself from being a party to the offence?



Directors' report

- Contents of Directors' report greatly enhanced
- Also importantly a Directors' Responsibility Statement – almost the same as Sarbanes Oxley

Independent directors

- Defined in sec 149 (6)
- Definition way more narrow as compared to the definition in clause 49 – hence may disqualify most of existing independent directors
 - No pecuniary relationship
 - Clause 49 language is “material pecuniary relationship”
 - Clause travels back in time to 2 previous financial years
 - Evidently, IDs may have had non material pecuniary transactions over the past
 - The provision will therefore be retroactive and will affect existing positions
 - Bar includes subsidiary, holding and associate companies as well
- Term of office 5 years
 - May be reappointed by another 5 years on special resolution
 - Not beyond that
 - Thereafter, may come back on board after a gap of 3 years
- **Data bank of independent directors**
 - Optional selection from panel of independent directors
- Existing companies given 1 year from the date of notification of the rules in this regard
- **Code for independent directors**
 - Massive code has been laid down in Schedule IV for independent directors

Proposals of SEBI on Independent Directors (IDs) in Concept Paper

Letter of appointment to IDs and NEDs

- The letter should specify:
 - The term of the appointment;
 - The expectation of the Board from the appointed director; the Board-level committee(s) in which the director is expected to serve and its tasks;
 - The fiduciary duties that come with such an appointment along with accompanying liabilities;
 - Provision for Directors and Officers (D&O) insurance, if any,;
 - The Code of Business Ethics that the company expects its directors and employees to follow;
 - The list of actions that a director should not do while functioning as such in the company; and
 - The remuneration, including sitting fees and stock options etc, if any.
- The Concept Paper proposes to align Clause 49 with the Bill



Training for independent directors

- This may be inserted as a non-mandatory requirement
 - Goes by OECD principles on corporate governance
 - Training may be imparted by recognised institutes

Age restriction and number of directorships of IDs

- SEBI puts up a proposal for discussion whether there should be age limits for independent directors
 - Schedule XIII provides for age limit of 25-70 in case of appointment of managerial personnel
 - Companies Bill incorporates the same as a part of the statute
- SEBI has proposed to put a cap on max no of directorships
 - Companies Act: 15
 - Bill – proposed limited : 10
 - MCA voluntary guidelines : 7

Tenure of independent directors

- Clause 49 to be amended to align with the Bill
 - Bill provides for tenure of 5 years + 5 years
 - Non mandatory requirements of Clause 49: 9 years
 - MCA voluntary guidelines: 6 years



Disclosure of reasons for resignation

- Existing clause 49 requires appointment of a person in place of a resigning/removed ID within 180 days
- IDs will not be required to give reasons for resignation
 - Submitted to the Board
 - Circulated by the company to shareholders
 - And to the stock exchange
- The provisions are by and large aligned with the Bill
- A director may not be allowed to use vague statement such as “personal reasons”
 - If he does so, he may will need to explain why those personal reasons do not compel him to resign from other boards as well



Compensation for IDs

- As is matter of common knowledge, Companies Bill bars all compensation in case of IDs
- Clause 49 encourages a balance between risk /reward

Performance evaluation of IDs

- Companies Bill requires performance evaluation of IDs to be done by the board
- SEBI proposes the evaluation should also be based on contribution as well as participation in board meetings
- The report should be placed before the Nomination Committee

Lead ID

- The proposal for a senior or lead ID has been discussed by SEBI in light of international regulations.
- Where the Chairman is an independent, the chairman will be treated as the senior
- Otherwise, the position will be rotated every 3 years
- Relevance
 - There are several occasions where there is a meeting of independent directors – such person chairs the meetings
 - Otherwise, coordinates the activities of IDs

Separate meetings of IDs

- Companies Bill provides for at least 1 separate meeting of IDs every year
- Clause 49 to be amended to provide for the same
- Specifically, these meetings shall discuss internal control, general governance practices
- And shall report the same to the general meeting
- Such meetings shall also review the performance of non-independent IDs

Duties of directors- in Bill

- The law lays statutory duties of a director
- Important duties
 - act in accordance with the articles of the company
 - due and reasonable care, skill and diligence and to exercise independent judgment
 - act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the stakeholders (company, employees, shareholders, etc.)
 - Avoid conflict of interest (with that of the Co.)
 - not achieve or attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates
 - not assign his office and any assignment so made shall be void
- Penal Provision: Minimum fine of Rs. 1 lakh, extendable to Rs. 5 lakh.

Vacation and Resignation of Directors

- **Vacation of office by directors**

- From the existing time limit of 3 months, the vacation of office for not attending board meetings is going to 12 months

- **Resignation of directors:**

- For the first time, law has inserted a mandatory provision for resignation
- A director may resign by notice
- The board *shall* take notice of the same
 - In other words, it is not mandatory for the resignation to be accepted
 - It is also explicitly provided that the resignation dates back to the date of receipt of the notice by the director

Board meetings

- Not more than 120 days gap between any consecutive board meetings
- 7 days notice prescribed
- Powers to be exercised at board meetings
 - The list of matters which require board meetings greatly expanded
 - Total 10 matters specified
 - And power to specify more matters



Restrictions on powers of directors



General Meeting Sanction, by Special Resolution

- Lawmakers have liberally gone on insisting on special resolution for every matter
- Sec 293 currently requires ordinary resolution
- Sec 180 insists on special resolution for the same matters
 - Even borrowing in excess of net worth also requires special resolution
- Meaning of “undertaking” defined
 - Undertaking in which the investment of the company is 20% or more, or turnover is 20% of the total income of the company
 - That is, it has to be an undertaking, and also to cross the limits mentioned above



Political Contributions &

Restriction on Power of Directors

- **Political contributions legalised**
 - Sec 182 legalises political contributions
- **Restrictions on powers of directors**
 - **Directors interests –**
 - Unlike existing sec 297 where consent of the CG is required for contracts with directors' interests, sec 184 merely requires disclosures
 - **Forward contracts on securities**
 - This is also a new restrictions
 - Language is though not clear but seems to prohibit forward contracts and option contracts in shares or debentures of the company, holding/subsidiary companies, or associate companies

Loan to Directors (Clause 185)

- Loans to directors generally barred, but may be given in pursuance of a scheme sanctioned by a special resolution
- No need for CG sanction
- Exemptions applicable to only:
 - Loan to MD or WTD
 - As per company's policy applicable to all employees
 - Pursuant to any scheme approved by way of an SR
 - Loans extended in ordinary course of business and interest at prevailing bank rate has been charged
- Severe penalty on non compliance:
 - Fine of minimum 5 lakhs which can extend up to 25 lakhs in case of companies
 - Loan receiver are punishable fine of minimum 5 lakhs which can extend up to 25 lakhs or imprisonment up to 6 months or both

Restrictions on powers of directors

- **Investments**

- Investments with not more than 2 layers
 - Act has prospective effect, existing investments will not be covered
- Loans and investments to be limited to 60% of net worth or 100% of free reserves and premium, unless sanctioned by a special resolution
- Rates of interest on loans linked with yields on G-secs of 1, 3, 5 or 10 years, closest to the terms of the loan
- NBFCs exempted – companies engaged in financing of companies – exempted
- Investment companies exempted from limits on acquisition of shares
- Holding and wholly owned subsidiaries also covered now and shall be included in limit of the clause

- **Non-cash transactions**

- New restrictions
- Any non-cash transactions with directors – acquisition of any asset by the company from the director, or vice versa, for consideration other than cash, requires general meeting resolution
- Section covers transactions with associates, subsidiary, connected persons



Related Parties and Related Party Transactions

- Definition becomes very very wide indeed.
 - Definition now as per accounting standard
 - Includes family members of HUF
- Merely holding of 2% of capital in public companies by a director makes the company a related party
 - Definition at par with sec. 299, but sec 299 is merely a disclosure requirement
- Related party transactions under the law are subject to serious restraint

Related Party Transactions

- Most transactions that a company may have with “related parties” require approval of board
- In case of companies of such size as may be prescribed, they further need approval by Special resolution
 - CG approval dispensed with
 - However, in the general meeting the member or his related party shall not vote

Abusive RPTs as provided in SEBI Concept Paper

- Real concern in closely held companies.
- Two modes for regulating RPTs:
 - approval based controls which require approval by Board of Directors/ Shareholders
 - disclosure based controls required under AS-18.
- Focus is on making disclosure norms effective

Proposals by SEBI to curb abusive RPTs

- Abuse by controlling shareholders by divesting the major subsidiaries without proper valuation to the companies indirectly owned by them
 - Proposal to require approval by shareholders for divestment of major subsidiaries
- Immediate and continuous disclosures of material RPTs
 - can be mandated by amending the reporting requirements specified under the LA
 - Suitable threshold limits for the reporting requirements need to be analyzed
 - Presently, requirement is to disclose annually

Proposals by SEBI to curb abusive RPTs (contd..)

- Shareholders/Share subscription or investment agreement sometimes gives superior rights to investors with ‘drag along rights’ or ‘tag along rights’.
 - Case of Messer Holdings Limited, Bombay High Court on September 1, 2010 which hold such consensual agreements to be legally valid.
 - Concept Paper proposes to examine whether listed company should be permitted to enter into such an agreement granting superior affirmative rights to selective investors.
- Approval of major RPTs by ‘Majority of the minority’
 - Clause-188 of the Companies Bill, 2012 contains a similar provision prohibiting interested shareholders from voting in Related Party Transaction approvals.
 - Provisions of listing agreement need to be aligned with the Bill

Proposals by SEBI to curb abusive RPTs (contd..)

- Pre-approval of RPTs by Audit Committee and encouraging them to refer major RPTs for third party valuation
 - The bill contains such provisions, LA needs to be altered in line with this
- Approval of Managerial Remuneration beyond a particular limit by disinterested shareholders
 - Most companies are managed by promoters and this brings in the concern of excessive managerial remuneration to executives forming part of promoter/promoter group
 - Clause 188 of Bill prohibits interested shareholders from voting in RPTs
- Expanding the scope of RPTs
 - Definition in *Ind-AS 24* to be adopted for LA requirements also



Insider Trading

- Provisions incorporated in the law
- Surprisingly, the section seems to be applicable to all companies – listed or unlisted
- Surely enough, there would not have been an intent to apply the section to unlisted companies



Managerial personnel and committees

Managerial Personnel

- Conditions of Schedule XIII incorporated in the law
 - This has a wrong impact – Schedule XIII pertains only to remuneration; such that where there is no remuneration, there is no need to apply the conditions
- However, now that the conditions have been incorporated in the law, they become mandatory in all cases
- For example, age limits in case of MD

Bar on appointment of Chairperson and managing director

- Sec 203, in a rather confused language, puts a bar on appointment of a Chairperson and the Managing director
- However, the section is not properly understood
 - As it stands, the bar is only on appointment as Chairperson by articles, and the managing director/CEO at the same time
 - That is, if the articles name the person as Chairperson, he cannot be appointed as MD
 - The section does not apply to a multi-business company
 - Multi-business issue to be detailed in rules to be framed

Managerial remuneration

- Several new concepts in Schedule V
- First, the ceilings of minimum remuneration hiked upto Rs 60 lacs
 - May be taken to Rs 120 lacs with special resolution
- Linkage with profits brought even in case of minimum remuneration
 - 2.5% of profits, or 5% with special resolution
 - This may actually be meaningless in case of loss or inadequacy
- Concept of payment by any other company (obviously group company) introduced
 - Provided the remuneration is within limits for that company
- New companies – within 7 years of incorporation
 - Limits are doubled
- So, the scope for CG approval is greatly reduced

Committees of the Board

- The following committees become statutory for every listed company
 - Audit committee: majority independent
 - Nomination and Remuneration Committee: only non-executive directors, at least half independent
 - Stakeholders Relationship committee (companies having 1000 or more shareholders)
: non executive chairperson
 - CSR committee: at least one independent



Secretarial audit and secretarial standards

Secretarial Audit and Secretarial Standards

- Secretarial audit to be mandatory in such companies as the rules may prescribe
- Secretarial standards generally become mandatory, as the definition of company secretary enjoins him to enforce the standards
 - Sec 205

Company Secretary

- Additional responsibilities come on the company secretary, as the CS is defined as a KMP.
- From administrative or ministerial person – becomes managerial person
- “officer in default” includes KMP – current provision in sec 5 also includes



Corporate social responsibility



Corporate Social Responsibility (CSR)

- This was highlighted as if it was the key feature of the Bill
- Section 135 deals with CSR – has 3 important elements
 - CSR Committee
 - CSR policy
 - CSR spending



Corporate Social Responsibility (CSR) (contd.)

- CSR Committee
 - Every company with either of these 3
 - Net worth of Rs 500 crores or more
 - Turnover of Rs 1000 crores or more
 - Net Profit of Rs 5 crores or more
 - Lots of issues left gray – net profit is profit before tax or after tax? Presumably it should be profit before tax
 - Referring to turnover and profits, the law says : “during any financial year” – surely enough, it cannot mean the running financial year. However, the law has not used “during preceding financial year” or during “any of the ** preceding financial years”
 - Clearly, the language is very very loose
 - CSR Committee to have at least 3 directors, of which at least 1 independent
- CSR Policy to be framed by the Board and put on the website of companies
- CSR spending
 - At least 2% of average profits for last 3 financial years to be spent on CSR
- The law does not specify what activities will be counted towards CSR – this is left for the CSR Committee

Some general questions on CSR

- Whether expenditure on staff, employees to be treated as CSR activities?
 - Bill provides to spend on social projects and expense on own employees cannot be treated as social services, hence, not allowed
- Can donation be given to group charitable organizations engaged in CSR?
 - Bill is silent. Can be given
 - May be a related party transaction if attracting the clause
- Can donation be given to outside charitable organizations with direction to spend in CSR?
 - Yes, can be given



Issue of securities

Issue of Securities

- Provisions for issue of securities seemingly rationalised, with a more logical distribution
- 3 types of security issuances
 - Public offer, that is, initial public offer, further public offer, or offer for sale
 - Private placement
 - Bonus or rights offers
- Contents of prospectus laid down in the section itself
- Prospectus
 - Full prospectus
 - Abridged prospectus
 - To be accompanied with every application form
 - Red herring prospectus
 - Prospectus containing all other details except quantum and pricing of the issue
 - Shelf prospectus
 - A prospectus that is supposed to remain on shelf, that is, alive for a long time, with particulars of changes in financial position filed periodically



Private Placements

- A complete part dedicated to private placements – sec 42
- Process of private placements greatly tightened – every offer of securities other than public, rights or bonus offer amounts to a private placement and governed by the section
- **Deemed public offer:**
 - to a number of investors being 50 or above, or such higher number as the CG may prescribe, shall be deemed to be public offer
 - **No exception in case of NBFCs** – may be the CG may prescribe a higher number
 - **Every private placement not complying with the requirements of the section**
- **Bombshell**
 - **Provisions about private placements applicable to private companies too – clear from the language of sec 23 (2)**
- **Provisions applicable to all private placements: extreme extent of tightening up – obviously thanks to Sahara ruling**
 - Every private placement to be made by way of an offer letter – 42 (1)
 - No further issue of securities unless previous securities offer allotted or offer withdrawn or abandoned
 - That is, if there are unallotted applications out of past issues, one cannot invite further applications
 - No applications in cash - cheque, DD or banking channels is the only way for issue of securities

Private Placements (contd.)

- Allotments to be made within 60 days
- If not allotted, money to be refunded within 15 days
 - If not refunded within 15 days, interest to be paid at 12%
- Monies raised by the issue will need to be parked in a separate bank account and cannot be used until allotted
- **In essence, the amendments made in Dec 2011 to Unlisted Public Cos. Preferential Issue of Securities rules incorporated into the law**
 - **This is a huge problem, since the section apparently applies to private companies as well**
- In addition, for every private placement, the company has to prove that the company had the names of the each of the recipients of the offer
 - And the offer will be addressed by name
- Additional compliance
 - Particulars of every private offer shall be filed with the Registrar within 30 days of circulation
- Penalty – amount involved in the offer, or Rs 2 crores – **whichever is higher; plus refund the money**

Types of Shares

- Types of shares
 - In case of private companies, there was no restriction on any type of shares
 - It was common for companies to issue management shares with disproportionate voting rights
- The new law applies to both public and private companies, and says, shares only to be of 2 types – equity and preference
- Within equity, it may be with disproportionate rights, but only in accordance with rules
- So private companies also come within rules for shares

Types of Shares (contd.)

- This may be tough for private equity investors who are used to disproportionate voting rights
- Not clear as to what happens to existing capital – obviously grandfathered
- In case of preference shares, several changes
 - Period goes up to 20 years
 - Distinction between cumulative and non cumulative pref shares goes as regarding voting rights for non payment of dividend
 - Provisions for premium payable on redemption
 - Premium to be paid from out of profits only in case of certain class of companies
 - Premium to be paid out of profits or securities premium in case of others

Transfer of Securities and Rectification of Register of Members

- Recognition of private contracts in relation to transfer of shares
 - A very strange proviso inserted below sec 58 (2) recognises contracts pertaining to transfer of shares
 - Obviously, the proviso relates to the ruling of the Bombay HC in *Messer Limited*.
 - However, does the proviso help at all?
 - There is no doubt that private contracts about transfer or restrictions on transfer are valid
 - Question is, is this contract enforceable against the company?
 - The proviso merely says – contract shall be enforceable, without clarifying enforceable against whom?
 - Sure enough, no contract can be enforceable against the company unless the company is a party, or a confirming party, or the contract is a part of the constitutional documents

Transfer of Securities and Rectification of Register of Members

- After a long gap, the provisions for rectification of register of members (sec 155 of the present Act) are back in the statute book
 - This was an agonising gap, as sec 111/111A did not have analogous provisions, and in several cases, courts have lamented the gap
 - Some courts held the power is with Civil courts
 - Now the power is back with the NCLT

Bonus Shares

- A very strange set of conditions has been stipulated for bonus shares in sec 63
- A company cannot issue bonus if the company has
 - Defaulted in payment of deposits or debt securities
 - Defaulted in payment of debt securities
- First, it is not sure from language whether default is current default, or past default as well
- Second, there is no reason to stop the issue of bonus shares for defaulted companies
- In fact, bonus issue conserves and augments the capital of the company and ensures the reserves becomes unavailable for distribution
- If bonus is not issued, the reserves are free for distribution, further adversely impacting the interest of the creditors

Issue of Debentures

- Provisions of sec 71 on issue of debentures are flawed
- Sub-section (4) says – “Where debentures are issued by a company under this section”, the company shall create a DRR
 - It may be noted that the requirement for DRR is without specifying how much DRR, over what period, etc. All this is left to be enacted in form of Rules.
 - Bigger issue is – the way the language stands, only debentures issued under sec 71 will need DRR
 - Debentures issued u/s 71 include convertible debentures and secured debentures
 - This may mean that for unsecured debentures, there is no requirement for DRR
 - This is completely counter-intuitive, since, actually, DRR is not required for convertible debentures



Deposits

Deposits

- Section not applicable in case of banking companies and NBFCs
 - Hence, NBFCs will continue to be governed by RBI directions
- In case of all other companies – there are 2 classes of deposits – members deposits and public deposits
 - As regards members deposits
 - Registered circular needed for deposits
 - Provision for deposit redemption reserve
 - Also provision for deposit insurance
 - All existing deposits to be paid within 1 year from the date of commencement of the Act

Deposits (contd.)

- Public deposits – sec 76
 - Separate section deals with public deposits
 - Only public companies may raise public deposits
 - CG to lay down rules about net worth and turnover, that is, eligibility to accept deposits from non-members
 - However, 2 substantial changes
 - Every company gets itself rated – no prescription as to what such rating should be
 - The company creates a charge on its assets, to the extent of amount of deposits



Charges

Charges

- List of registrable charges eliminated
 - This is actually not proper
 - For example, a pledge does not require registration as it is possessory interest
- Registrar's power to extend registration of charge extended to 300 days – that is, 30 days + 270 days
- Completely creditor-driven registration of charge allowed – sec 78 – if the company does not register within the time frame of the law



Filing requirements



Annual Return

- Contents of annual return extended substantially
- AR to be signed by a practising company secretary in all such cases where there is no secretary
- AR of every listed company, and a company having such size as prescribed, requires certification by a PCS



Additional Filing Requirement:

Changes in Promoter Shareholding

- In case of all listed companies, Changes in shareholding of promoters, and top 10 shareholders, to be filed within 15 days
 - The requirement applies to any change in top 10 shareholders' holdings
 - Therefore, companies will have to track the top 10 holders' holdings on a daily basis, to report any changes
- This is on top of requirements under the Insider Trading Regulations



Investigations

Freeze on assets

- A very important power is conferred by sec 221 to freeze several things
- To be triggered on
 - Reference by CG
 - Any members entitled to apply against oppression
 - Creditors entitled to Rs 1 lac or above
- Apprehensions
 - the removal, transfer or disposal of funds, assets, properties of the company is likely to take place in a manner that is prejudicial to the interests of the company or its shareholders or creditors or in public interest
- The same may be injuncted



Meetings



Meetings

- AGM cannot be called on a “national holiday”
 - This might mean AGM can be called on a Sunday
- Quorum for meetings
 - Age-old rule changes – quorum is based on number of shareholders
 - Private companies – 2
 - Public companies
 - Upto 1000 shareholders – 5
 - 1000 – 5000 - 15
 - More than 5000 – 30

Meetings (contd.)

- **Postal ballot**
 - First of all, as against existing section, postal ballot made option for all companies – listed or unlisted
 - Second, postal ballot is optional in every case
 - Except in case of removal of auditors or directors
 - Third, postal ballot is mandatory for such matters as may be laid by Rules
- **Secretarial standards**
 - Become mandatory
 - Those regarding board and general meetings
- **Post-AGM report**
 - A new report is required to be filed by all listed public cos within 30 days of the AGM



Compromise, arrangements,
oppression, class action

Compromise and Arrangement

- The language of the section may seem to suggest that CDR by bankers will also come under the section
- However, that is not the case
 - Affidavit about a CDR has to be filed only where an application is made to the NCLT regarding a scheme or arrangement
- **Self approved mergers/demergers: Sec 233**
 - Mergers between 2 or more small companies
 - Holding and subsidiary companies
 - Such classes of companies as may be prescribed
 - May be done without approval of NCLT
- **Cross border mergers**
 - Section 234 provides for cross border mergers too

Oppression and Class Action

- **Oppression**
 - Mismanagement section seems to have been merged into oppression
 - This is actually not desired as these two are completely different remedies
- **Class action**
 - Concept of class action is present in some other sections too
 - Sec 37 in case of any offences in relation to security issuance
 - Sec 245 incorporates a broad so-called class action provision
 - Requisite strength of members is to be laid by rules
 - Deposits – at least 100
 - The earlier version of the Bill includes creditors as well - that has been omitted

Where does class action lie?

- (a) to restrain the company from committing an act which is *ultra vires* the articles or memorandum of the company;
- (b) to restrain the company from committing breach of any provision of the company's memorandum or articles;
- (c) to declare a resolution altering the memorandum or articles of the company as void if the resolution was passed by suppression of material facts or obtained by mis-statement to the members or depositors;
- (d) to restrain the company and its directors from acting on such resolution;
- (e) to restrain the company from doing an act which is contrary to the provisions of this Act or any other law for the time being in force;
- (f) to restrain the company from taking action contrary to any resolution passed by the members;
- (g) to claim damages or compensation or demand any other suitable action from or against—
 - (i) the company or its directors for any fraudulent, unlawful or wrongful act or omission or conduct or any likely act or omission or conduct on its or their part;
 - (ii) the auditor including audit firm of the company for any improper or misleading statement of particulars made in his audit report or for any fraudulent, unlawful or wrongful act or conduct; or
 - (iii) any expert or advisor or consultant or any other person for any incorrect or misleading statement made to the company or for any fraudulent, unlawful or wrongful act or conduct or any likely act or conduct on his part;
- (h) to seek any other remedy as the Tribunal may deem fit.



Valuers

- Qualifications to be laid down
- Registration requirements to be laid down



Miscellaneous



Sick companies



Sick Companies

- What is a sick company
 - Unfortunately the law does not define sickness with reference to loss of net worth or inability to pay
 - The law leaves sickness to be determined by the NCLT
- Who may make a reference
 - Secured Creditors with 50% or more outstanding debt who have unpaid debt after 30 days of notice
 - The company
 - CG or SG or PFI or a scheduled bank
- Moratorium
 - No automatic moratorium
 - However, NCLT may stay winding up, execution, distress or like against the property of the company, suit for recovery of money, or enforcement of security interest
 - Moratorium to apply for 120 days
- Stay on the company
 - Disposal of assets
 - Any decision which is adverse to creditors

Measures for revival

- The provisions are analogous to administration proceedings under UK insolvency law
- An interim administrator is appointed to preserve the assets and management of the company
- Interim Administrator appoints a committee of creditors
- The decision as to revival or winding up is based on decision of creditors



Other provisions



Mediation and Conciliation

- Sec 442 provides for power, in case of any proceeding before the NCLT or the CG or NCLAT, to refer a matter to the mediation and conciliation panel



Dormant Companies

- New class of companies to be formed for future transactions
 - Has no significant accounting transactions
 - That is, any transaction other than payment of fees, allotment of shares, statutory payments, payment to maintain office records
- Idea is to impose minimal requirements on dormant companies
 - Rules to be made in this regard



Depreciation

- From prescribed rates of depreciation, the law now provides for asset lives
 - Useful lives of assets are laid down
- A company may spread the cost of the asset, minus the RV, systematically over the useful life



New Powers to Professionals

- Lots of areas of Secretarial Audit
- Registered valuers
- Company liquidators
- Legal representative at NCLA and NCLAT may be CAs , cost accountants and CSs
- Mediation and conciliation Panel



frauds

- The word fraud is repeated 136 times in the Act
- Fraud is defined as any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss.
- In addition to any other liability, a person found guilty of a fraud shall be punishable with:
 - Imprisonment for a term up to 10 years; AND
 - If fraud involves public interest, term may extend to 20 years
 - Fine not less than the amount involved but may extend up to three times the amount involved in fraud



Serious Fraud Investigation Officers (SFIOs)

- SFIOs have powers to investigate into affairs of the company and is required to submit its report to CG
- Investigation can be initiated:
 - On receipt of RoC notice
 - On request of company by way of an SR
 - In public interest
 - On request of any department of central or state government
- Once SFIO investigation initiates, no other agency can proceed with investigation
- Company's officers, present and past employees to co-operate with SFIO and provide required information/documents etc



Non-bailable offences

Section	Subject matter
7 (5) & (6)	Furnishing false information at the time of incorporation of a company
34	Prospectus issued with false or misleading information
36	False or deceptive statement/promise to induce another person to invest
38(1)	Person making application to company for subscribing to its shares in fictitious or multiple name
46(5)	Companies issuing duplicate share certificates with an intent to defraud
56(7)	Wrong transfer of shares by depository or DP with an intent to defraud

Non-bailable offences contd..

Section	Subject matter
66(10)	Any officer who, at the time of reduction of share capital, conceals name or amount of debt of a creditor
140(5)	If Tribunal is satisfied that an auditor has acted fraudulently or colluded in fraud, such auditor, whether individual or firm, shall be punishable
206(4)	If RoC, on inspection, is satisfied that company is carrying on for a fraudulent or unlawful purpose
213	If on investigation, Tribunal finds any fraud
229	Any person providing wrong information or destroying or tampering with any document at the time of inspection/investigation
251(1)	Fraudulent application by company for striking off name
339(3)	Any person who is knowingly a party to carrying on business in fraudulently manner
448	Any person giving false material particulars in any statement, return or certificate

Reporting by SFIO

- Persons punishable with cognizable offence may be released on bail only if:
 - Public Prosecutor has been given an opportunity to oppose the application for such release
 - On satisfaction of court that he is not guilty of such offence and that he is not likely to commit any offence while on bail
- Following are not punishable:
 - Woman
 - Minor under the age of 16
 - Sick or infirm person
- Report filed by SFIO to be treated as report filed by police u/s 173 of CrPC for framing charges
- SFIO can also investigate under existing Act



One person companies



One Person Companies (OPCs)

- **Definition:**
 - “One Person Company” (OPC) means a company which has only one person as a member. [Clause 2(62)]
- A company may be formed for any lawful purpose by one person, where the company to be formed is to be OPC i.e., a private company, by subscribing his name to a memorandum and complying with the requirements of this Act in respect of registration [Clause 3(1)(c)]

OPCs: Privileges

- The financial statement may not include the cash flow statement [Clause 2(40)]
- The annual return to be signed by the company secretary, or where there is no company secretary, by the director of the company.
- No requirement of holding an AGM [Clause 96(1)]
- Provisions not applicable as per Clause 122(1): Section 98 [Power of Tribunal to call meetings of members, etc.] and Sections 100 to 111 (both inclusive) [Calling of EGM, notice, explanatory statement, quorum, chairman, proxies, restriction on voting rights, voting methods, postal ballot, circulation of members' resolution]



OPCs: Privileges (Contd. 1)

- For ordinary business:
 - The resolution (ordinary/special) to be communicated by the member to the company and entered in the minutes-book (under section 118) and signed and dated by the member;
 - Such date shall be deemed to be the date of the meeting for all the purposes under this Act. [Clause 122(3) read with sub-clause (2)]
- For any business to be transacted by BoD of the Company, where there is only 1 director:
 - The resolution to be entered in the minutes-book (under section 118) and signed and dated by the director;
 - The date shall be deemed to be the date of the meeting of the Board of Directors for all the purposes under this Act.



OPCs: Privileges (Contd. 2)

- The financial statement, including consolidated financial statement, if any, to be approved by the Board of Directors before they are signed on behalf of the Board only by one director, for submission to the auditor for his report thereon. [Clause 134(1)]
- A copy of the financial statements duly adopted by its member, along with all the documents which are required to be attached to such financial statements, is to be filed within 180 days from the closure of the financial year. [Proviso to Clause 137(1)]. For companies other than OPC, the cut-off date for filing is 30 days from the date of AGM.



OPCs: Privileges (Contd. 3)

- Minimum number of directors: 1 [Clause 149(1)]
- Meeting of Board:
 - At least one meeting of the Board of Directors in each half of a calendar year and
 - the gap between the two meetings not less than ninety days. [Clause 173(5)];
 - not applicable where there is only one director.
- Clause 174, regarding Quorum for Board Meetings not applicable where there is only 1 director in OPC.



OPCs: Other Important Points

- Memorandum to indicate the name of the other person, with his prior written consent in the prescribed form, who shall, in the event of the subscriber's death or his incapacity to contract become the member of the company; the written consent of such person to be filed with the Registrar at the time of incorporation of the OPC along with its memorandum and articles:
 - other person may withdraw his consent in such manner as may be prescribed:
 - the member of OPC may at any time change the name of such other person by giving notice in such manner as may be prescribed:
 - duty of the member of OPC to intimate the company the change, if any, in the name of the other person nominated by him by indicating in the memorandum or otherwise within such time and in such manner as may be prescribed, and the company shall intimate the Registrar any such change within such time and in such manner as may be prescribed



OPCs: Other Important Points (contd. 1)

- Memorandum to state:
 - the name of the person who, in the event of death of the subscriber, shall become the member of the company.[Clause 4(1)(f)]
- The words “OPC” shall be mentioned in brackets below the name of such company, wherever its name is printed, affixed or engraved. [Proviso to Clause 12(3)]
- The report of the Board of Directors to be attached to the financial statement under this section shall, in case of a OPC, mean a report containing explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made by the auditor in his report.[Clause 134(4)]



OPCs: Other Important Points (contd. 2)

- In the absence of any provision in the Articles of Association for the appointment of first director, the member of OPC himself is deemed to be the first director until the director or directors are duly appointed by the member in accordance with the provisions of this section. [Clause 152(1)]
- Contracts between OPC (limited by shares or guarantee) and sole member + the director of the OPC, if not in writing: OPC to ensure that the terms of the contract or offer are contained in a memorandum or are recorded in the minutes of the first meeting of the Board of Directors of the company held next after entering into contract; not applicable to contracts entered in the ordinary course of business. [Clause 193(1)]



OPCs: Other Important Points (contd. 3)

- Memorandum of Association:
 - 7th Clause only applicable to OPC where the sole member agree to take all the shares in the capital of the company;
 - 8th Clause for nominee in the event of death of the sole member
- TABLE F: AoA of Company limited by shares:
 - For transmission of shares- the nominee to have title to all the shares of the member on the death of the sole member;
 - to be informed of the event by BoD;
 - nominee shall nominate any other person with the prior written consent of such person who, shall in the event of the death of the member, become the member of the company.



Small companies

Meaning of small companies

- Private company [Clause 2(85)].
- Not being
 - holding company or a subsidiary company;
 - a company registered under section 8 (companies with charitable objects);
 - or a company or body corporate governed by any special Act.
- Maximum **paid-up share capital** Rs. 50 lakhs (higher amount may be prescribed but in any case, not to exceed Rs. 5 crores) [Clause 2(85)(i)]
- Maximum **turnover** as per last P/L A/c of Rs. 2 crores (higher amount may be prescribed but in any case, not to exceed Rs. 20 crores [Clause 2(85)(ii)]



Privileges

- Financial Statement may not include **cash flow statement**. [Proviso to Clause 2(40)]
- **Annual Return** to be signed by the CS or where there is no CS, by the director of the company [Proviso to Section 92(1)]. In other companies (other than OPCs, and small companies), the annual return is to be signed by a director and the CS, or where there is no CS, by a CS in practice.
- Board meetings: Minimum 1 meeting in each half of a calendar year; minimum gap between 2 meetings is 90 days [Clause 173(5)]. Therefore, the general requirement of minimum 4 Board meetings and maximum gap of 120 days not applicable.
- **Self approved mergers:** Conditions for a scheme of **merger or amalgamation** may be entered into between two or more small companies: Clause 233(1), non-obstante clause- overrides Clauses 230 (Power to compromise or make arrangements with creditors and members) and 232 (Merger and Amalgamation of companies).



Charitable Companies

Companies not for profit

- Any person or association of person can apply with:
 - objects of promotion of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment or any such other object
 - Intending to apply its profits in promotion of objects and
 - Prohibit to pay any dividend to members
- Such Companies to enjoy all the privileges and be subject to all the obligations of limited companies
- A firm can be a member of such companies
- All other conditions are same as are there in existing Act
- If proved that the affairs of company conducted fraudulently, every officer is punishable under clause 447

THANK YOU