

AN INSIGHT ON Companies (Amendment) Act, 2017

“Integrating Growth & Governance “

RAJKOT – JUNE 17, 2018

S.SUDHAKAR

VICE-PRESIDENT – CORPORATE SECRETARIAL

RELIANCE INDUSTRIES LIMITED

Disclaimer

Views expressed are of my own and not of the organisation in which I am employed

This presentation is as per my understanding of the Amendment Act

History

- **Companies Act, 2013 was one of the most significant reforms brought out in the recent past**
- **The Act has elevated the standards of compliances, disclosures, accountability, investor protection and corporate governance measures**
- **Several significant implementation challenges**
- **Constitution of Company Law Committee**

History

- Companies (Amendment) Bill, 2016 was introduced in the Lok Sabha on March 16, 2016
- Referred to standing committee in April 2016 which has presented its report in December, 2016
- Companies (Amendment) Bill, 2017 was approved by Lok Sabha on July 27, 2017
- Companies (Amendment) Bill, 2017 was passed by Rajya Sabha on December 19, 2017
- President's assent was received on January 3, 2018

Notifications of Amendments

- As per the Amendment Act, Central Government can notify different dates for different provisions
- Sections 1 and 4 were notified on January 26, 2018
- About 42 sections were notified on February 9, 2018
- Further approximately 25 sections were notified on May 7, 2018
- Another 5 more sections were notified on June 13, 2018
- Approximately 22 more sections are still to be notified

Purpose of the Amendments

- To Simplify the Law, eliminate redundancies, provide clarity for provisions which are considered to be ambiguous
- To address the difficulties in implementing owing to stringent compliance requirements
- To facilitate ease of doing of business in order to promote growth with employment and encouragement of start-ups
- Harmonisation with accounting standards, SEBI and RBI Acts and Regulations there under
- Rectifying omissions and inconsistencies in the Act
- Strict action against defaulting companies
- To give effect to the recommendations of the Company Law Committee

Rationalisation of penal provisions

- The Amendment Act has provided the penal provisions which are commensurate to the gravity of the offence
- Considering the following penal provisions have been provided / amended
 - the offence
 - injury to public interest
 - nature and gravity of default
 - repetition of default
 - size of the company
 - nature of business

AMENDMENTS

Amendments

- The bill provides for a total of over 96 amendments
 - 3 new sections were inserted
 - 5 sections were substituted
 - 3 sections were omitted
- Remaining were amended

Insertions of new sections

- 3A – members severally liable in certain cases
- 446A – factors for determining level of punishment
- 446B – lesser penalties for one person companies and small companies

Sections substituted

- 42 - issue of securities on Private placement basis
- 90 - register of significant beneficial owners
- 185 – Loans to Directors
- 406 – provisions relating to Nidhi companies
- 435 – establishment of special courts

Omissions

- 93 - return to be filed in case promoter stake changes
- 194 – prohibition of forward dealings in securities
- 195 – prohibition of insider trading of securities

Major changes

- Changes in definitions – associate company, subsidiary company, related party, turnover and net worth
- Private placement process
- Provisions relating to Loans to Directors
- Replacement of Central Government approval for managerial remuneration
- Alignment of disclosure provisions in prospectus with SEBI regulations

DEFINITIONS

2(6) Associate Company

- Associate company means a company in which the other company has a significant influence, but not a subsidiary company and includes a joint venture company
- By virtue of the definition to become an ‘associate’ the other entity should be a ‘company’. Hence a body corporate can’t be an associate
- Significant influence means -
 - “control of at least twenty per cent of total ~~share capital~~ voting power or control or participation in business decisions under an agreement”
- Control is defined under section 2(27)
- *The definition of Associate company is substantially widened*

2(6) Joint Venture

- As per the Act 'Associate' includes a joint venture company
- Now 'Joint venture' is explained in an explanation to Section 2(6)
- Joint venture means –
 - “a joint arrangement whereby the parties that have joint control of the arrangement have right to the net assets of the arrangement”
- *To a large extent definition of 'Associate' and 'Joint Venture' are aligned with Accounting Standards*

2(30) Debenture

- Section 2(30) defines 'Debenture' to include debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a debt or not
- This made the definition very wide and by implication **covers instruments like commercial papers, derivatives and other money market instruments**
- The proposed amendment added a proviso under which the following are excluded
 - the instruments referred to in Chapter III-D of the RBI Act, 1934 and
 - such other instruments prescribed by the Central Government in consultation with the RBI
- *This amendment has given clarity and removed the ambiguity, if any*

2(41) Financial Year

- NCLT has the authority to allow a company or a body corporate, which is a subsidiary or holding company of a company incorporated outside India, to follow a different financial year, if it is required to do so, for consolidation of accounts outside India.
- NCLT has no authority to allow an ‘associate company’ to do so
- Now NCLT can allow an ‘associate company’ (being an Indian company) of a company incorporated outside India, to adopt a different financial year
- Since associate company includes a JV company, such company too can approach NCLT to adopt a different financial year
- *This enables ‘associate companies’ too to approach NCLT to follow a different financial year*

2(46) Holding Company

- Holding company is defined as “a company of which such companies are subsidiaries”
- Hence to become a holding company, the entity is to be a company and not a body corporate
- The explanation to section 2(87) clarifies the expression ‘company’ includes any ‘body corporate’. Similar explanation was not there in section 2(46)
- **This was a minor anomaly.**
- The amendment act has provided similar explanation as that of Section 2 (87)

2(49) Interested Director

- Though the definition is very wide, the only reference given to this is in Section 174(3) i.e. for the purpose of quorum
- Here also in the explanation it was provided that the term 'interested director' means, a director within the meaning of Section 184(2)
- Considering the redundancy, **this definition is omitted**

2(51) Key Managerial Personnel

- The following category of KMP is introduced
- “such other officer,
 - not more than one level below the directors
 - who is in the whole-time employment
 - designated as KMP by the Board
- *This amendment enables the companies to make the senior officials accountable for the compliance of the provisions of the Act*

2(57) Net worth

- ‘Net worth means the aggregate value of the paid-up share capital and all the reserves created out of the profits and securities premium account
 - Earlier there was an ambiguity in regard to the debit / credit balance of the P&L account.
- Now the clarity was provided with the amendment as under
 - Net worth means “paid up share capital and all reserves created out of the profits, securities premium account and debit or credit balance of profit and loss account”

2(76) Related Party

- In sub-section (viii) of section 2(76) – ‘any company’ has been replaced with ‘any body corporate’
 - with this a company which is incorporated outside India which may be a holding, subsidiary or **associate company** becomes a Related party
 - Company includes body corporate only in case of the definitions of Holding and Subsidiary companies and not for Associate company.
- The following is added to Section 2(76) (viii)
- “an investing company or any venturer of the company
- investing company or any venturer of the company means –
 - “A body corporate whose investment in the company would result in the company becoming an associate company of the body corporate” (i.e. **two way relation**)
 - **Earlier only associate company was related party and not the investor. This anomaly is removed**

2(85) Small company

- The limits are increased as under –
- Paid-up share capital – from Rs 5 crore to Rs 10 crore
- Turn over - from Rs 20 crore to Rs 100 crore
- Several companies can get the benefit of falling in the definition of 'small companies' and get the related privileges

2(87) Subsidiary company

- Subsidiary in relation to any other company means a company in which the holding company
 - Exercises or controls more than **one-half of the total share capital** either at its own or together with one or more of its subsidiary companies
 - Total share capital includes preference share capital
- In companies where in 'preference share capital' is greater than 'Equity', it becomes a subsidiary of the entity that holds preference shares, though they have no control or voting rights
- To avoid this absurdity, it was proposed to substitute the 'total share capital' with 'total voting power'
- As per section 47 where **dividend** in respect of a class of preference shares **has not been paid for a period of two years or more**, they **shall acquire right to vote** on all the resolutions placed before the company
- *With this amendment 'control and ownership' goes hand in hand*

3A Reduction in number of members -

- When such **reduction is below statutory limit** i.e. seven for public and two for private and
- The company **carries on business** for period of **more than 6 months**
 - **Every person who is a member** and is cognisant of the fact is **severally liable** for payment of the whole of the debts contracted during this time
- ***This was a lacuna in Companies Act, 2013, which is removed now***

PRIVATE PLACEMENT

42 Private placement – not yet notified

- Private placement may be made to a select group of persons who have been identified by the Board.
- Shall not be offered to more than 50 or such number of members as may be prescribed (excluding QIBs and employees of the company being offered ESOP)
- Private placement offer and application shall not carry any right of renunciation
- Subject to the maximum number of identified persons, a company may, at any time, make more than one issue of securities to such class of identified persons as may be prescribed
- Securities shall be allotted within 60 days from the date of receipt of the application money
- Issue proceeds shall not be utilised unless allotment is made and the return of allotment is filed with the ROC
- Return of allotment shall be filed with in fifteen days from the date of allotment

Penal provisions

- **Default in filing the 'return of allotment'** – promoters and directors shall be liable to a penalty of Rs 1,000 for each day not exceeding Rs 25 lakhs
- If the company makes an offer or accepts monies in contravention of the provisions, the company, its promoters and directors shall be liable
 - for a penalty which may extend to the amount raised or two crore rupees whichever is lower and
 - the company shall refund such monies
- Notwithstanding penal provisions, if the private placement is not made in compliance with the provisions
 - the issue shall be deemed to be a public offer and all provisions of Companies Act, 2013, SCRA and SEBI acts shall be applicable

SHARE CAPITAL & DEBENTURES

53 Issue of shares at discount

- Issue of shares at discount is void except as issue of sweat equity
- Sub-section (2) provide that ‘any share issued by a company at a **discounted price**’ shall be void
- The term ‘discounted price’ could be interpreted to mean a price lower than the market value of shares and not lower than its nominal value as intended.
- Hence the word ‘**discounted price**’ is replaced with the word ‘**discount**’
- To enable restructuring of a distressed company the following amendment is proposed
 - Company may issue shares at a discount to its creditors, when debt is converted into shares in pursuance of any statutory resolution plan or debt restructuring scheme in accordance with the guidelines or directions or regulations specified by RBI
- *The clarification and the relaxation given certainly facilitate the restructuring schemes of distressed companies*

54 Issue of Sweat Equity Shares

- According to sub-section 1(c) **one year period shall be elapsed** for issue of sweat equity shares from the date of commencement of business
- ‘commencement of business is not defined and it’s a challenge for companies to arrive at this
- The Amendment Act has removed the period of one year and permits companies to issue sweat equity within one year period also
- Hence sweat equity can now be issued at any point of time, after registration of the company
- *This amendment helps several start ups to issue Sweat equity without any waiting period in the initial crucial stages*

DEPOSITS

73 Acceptance of Deposits - (not notified)

- Not less than 20% of the deposits maturing during the following financial year shall be kept in a scheduled bank in a separate bank account called as “Deposit Repayment Reserve” account
 - earlier this was not less than 15% of deposits maturing during a financial year and the financial year next following - section 2(c)
- Provision relating to Deposit Insurance is omitted
- Where the default had occurred, the company made good the default and a period of five years had lapsed, since the date of the default, the company may accept deposits
 - earlier once default was occurred there was no relaxation and there was a life term ban
- The relaxation provided in Deposit Repayment Reserve account remove the stress on the liquidity of the companies and once the default is remideid the companies can again accept Deposits

76A Penal provisions

- In case of sub-clause (a) for failure to repay the deposits the company shall be punishable with
the penalty of **Rs one crore is replaced with “one crore rupees or twice the amount** which ever is lower (presently the fine extends up to Rs 10 crore)
In case of sub-clause (b) every officer of the company who is in default shall be punishable with
 - the words “imprisonment of seven years or with fine” is replaced with “seven years and with fine”
 - not compoundable
- *The proposed penal provisions certainly make the companies accountable and the officials responsible*

89 Beneficial interest – not notified

- Beneficial interest which is referred to in sections 89 and 90 is defined
- Beneficial interest in a share **includes**,
- directly or indirectly, through any contract, arrangement or otherwise,
- the right or entitlement of a person alone or together with any other person to
 - exercise or cause to be exercised any or all of the rights attached to such share; or
 - receive or participate in any dividend or other distribution in respect of such share

90 Significant Beneficial Ownership

- Concept of ‘Significant Beneficial Owner’ (SBO) has been introduced
- **Significant Beneficial Owner means;**
- **“every individual** who acting alone or together with one or more persons or trust, **(SBO is to be a natural person)**
- including a trust and persons resident outside India,
- holding beneficial interest of not less than 25% **or such other percentage** as may be prescribed in -
 - Shares of a company or the right to exercise or the actual exercising of significant influence or control over the company

SBO as defined under SBO Rules 2018

- The Rules defined 'significant beneficial owner' as under;
 - **an individual referred to in Section 90(1)** (holding ultimate beneficial interest of not less than 10%) read with Section 89(10)
 - but whose name is not entered in the ROM of the company, as the holder of such shares

SBO in case member is other than individual

- SBO in case of persons other than individuals or natural persons, shall be determined as under:
 - **Where the 'member' is a company** and SBO is a natural person, whether acting atone or together with other natural persons or through one or more persons or trusts, holds not less than 10% share capital of the company or who exercises significant influence or control in the company through other means
 - **Where the 'member' is a 'partnership firm'** and the SBO is a natural person whether acting atone or together with other natural persons or through one or more persons or trusts, holds not less than ten percent of capital or has entitlement of not less than ten percent profits of the partnership
- Where no natural person is identified under the above, the SBO is the relevant natural person who holds the position of senior managing official

In case member is a Trust

- **Where is the member is a Trust** (through trustee), the identification of the **beneficial owner (here the term SBO is not used)** shall include identification of the author of the trust, the trustee, the beneficiary with not less than 10% interest in the trust and any other natural person exercising ultimate effective control over the trust through a chain of control or ownership
- For the purpose of this clause instruments in the form of GDRs, CCPs or CCDs shall be treated as 'shares'

Declaration by SBO

- A **declaration is to be made** to the Company by the person who is a significant beneficial owner
 - within 90 days of commencement of the Rules or within 30 days of change of his SBO
 - within 30 days of acquisition of SBO
- Central Government may prescribe a class of companies who need not be required to make such declaration
 - Mutual Funds, Alternate Investment Funds (AIFs), Real Estate Investment Trusts (REITs), and Infrastructure Investment Trusts (InvITs) registered under SEBI Act are exempted

90 Register of Significant Beneficial ownership

- Every company shall maintain a **Register of interest** declared by individuals and changes therein
- Such register is **open for inspection** by any member of the company
- Every company shall **file a return of significant beneficial owners** of the company and changes therein with the ROC in such manner as prescribed
- Company shall give **notice to any person** in case it knows or has reasonable cause to believe that
 - he is the significant beneficial owner of the company;
 - he has knowledge about the significant beneficial owner
 - he is the significant beneficial owner during the preceding three years

Beneficial ownership contd

- Information required by the notice shall be given within a period not exceeding 30 days
- Where the person fails to give the information or information given is not satisfactory, company shall apply to Tribunal to impose restrictions with regard to transfer of interest, suspension of all rights attached
- Stringent penalties provided for default including liability for fraud under Section 447
- *Enhance transparency and identification of ultimate beneficiaries of shares*
- *Misuse of corporate vehicles for the purpose of evasion of tax, laundering money, corrupt or illegal purposes can be curtailed with this amendment by tightening the concept of beneficial interest*

MEETINGS

92 Annual Return - (not notified)

- In annual return 'indebtedness clause' is omitted
- Names, addresses, countries of incorporation, registration and percentage of shareholding **held by FIIs is omitted**
- Central government may prescribe **abridged form of annual return** for one person company, small company or such other class of companies as may be prescribed
- Extracts of annual return (MGT9) need not be annexed to the Board's report
- Place copy of the annual return on the website of the company, if any, and the web-link of such annual return shall be disclosed in the Board's Report
- Time limit prescribed under section 403 has been done away with.
- The proposed amendment simplifies the Annual Return and reduces the burden of publishing the extracts of annual return as part of annual report

96 & 100 General Meetings

- AGM of an unlisted company may be held at any place in India
 - If the consent is given by all the members in advance
- EGM of a company other than of the WOS of a company incorporated outside India, shall be held at a place within India
- Only WOS of a body corporate can hold its EGM outside India, but it has to hold its AGM in India only
- *This amendment certainly facilitates the companies to hold the meetings as per their convenience*

101 Notice of General meeting

- General meeting may be called by shorter notice if consent is accorded thereto
- In the case of AGM, by not less than 95% of the members entitled to voting thereat and
- In case of any other general meeting, by members of the company
 - if the company has share capital majority in number entitled to vote and who represent not less than 95% of such part of the paid-up share capital of the company as gives a right to vote at the meeting; or
 - if the company has no share capital, not less than 95% of the total voting power exercisable at the meeting
- If a member is entitled to vote on some resolutions and not on other resolutions, he shall be taken into account as per entitlement only

110 postal ballot

- In case of e-voting scenario postal ballot has lost its relevance for the companies which are mandatorily required to provide e-voting
- If a company is required to provide facility to vote by electronic means under section 108
 - It may transact the business required to be transacted by means of postal ballot at a General Meeting of the company
- This means that companies which are not required to provide facility of voting by electronic means,
 - they have to necessarily transact the business required to be transacted by postal ballot, by postal ballot only

DIVIDEND

123 Declaration of Dividend

- While computing profits the following shall be excluded
 - any amount representing unrealised gains, notional gains or revaluation of assets and any changes in carrying amount of an asset or of a liability on measurement of the asset or liability at fair values (new proviso to sub-sec 1)
- In the second proviso ‘transferred by the company to the reserves’, “reserves” shall be substituted by ‘free reserves’

Interim Dividend

- Board may declare interim dividend (new sub-section 3)
 - during any financial year or
 - at any time during the period from closure of the financial year till holding AGM
- Interim dividend may be declared
 - out of the surplus in the P&L account or
 - out of profits of the financial year for which such interim dividend is sought to be declared or
 - out of profits generated in the financial year till the quarter preceding the date of declaration of the interim dividend
- This means Board can declare interim dividend even after the closure of a financial year and from the profits of the current financial year
- Aforesaid provisions increased the ability of the Boards to declare interim dividend

Restriction on Interim Dividend

- In case the company incurred **loss during the current financial year** up to the end of the quarter immediately preceding the date of declaration of interim dividend
 - Such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during immediately preceding three financial years

FINANCIAL STATEMENTS

129 Financial statement

- Sub-section 3 is substituted
- The explanation to 129(3) stating that the word ‘subsidiary’ shall include ‘associate’ and ‘joint venture’, has been brought into the main sub-section (3) itself as under
 - Where a company has one or more subsidiaries or associate companies, it shall
- In the revised definition of ‘associate company’, joint venture is included
- The consolidated financial statements shall be in accordance with the applicable accounting standards
- In case a company has only a Joint venture and no associate or subsidiary – whether accounts are to be consolidated?
 - Since Joint Venture is included in the ‘associate’ definition and associate accounts are to be consolidated, JV accounts are to be consolidated

130 Re-opening of Accounts

- While passing orders for re-opening of accounts the court or the tribunal **shall also give notice to 'any other person concerned'**
 - This is **in the interest of principle of natural justice**, so that the other person who is concerned may submit their concerns before passing any orders
- **No order shall be made for re-opening of accounts relating to a period earlier than eight financial years**, immediately preceding the current financial year
- In case Central Government issue direction under section 128(5) for keeping books of accounts for a period longer than eight years, the books of accounts may be ordered to be re-opened within such longer period

134 Financial statement & Board report (not notified)

- Financial statement and consolidated financial statement **shall also be signed by CEO**
 - earlier CEO to sign only if he is on the Board
- Extract of annual return need not be attached to the Board's report. **Only web link is to be provided** wherein **copy of the annual return** was uploaded
- In the Board's report a statement is to be given indicating that, 'annual evaluation of the performance of the Board, its Committees and of individual directors **has been made**'
- Earlier this was '**evaluation has been made by the Board** of its own performance and that of its committees and individual directors
- **Disclosures given in the financial statements** shall be referred in the Board's report and need **not be repeated**

Board's Report contd...

- CSR and Remuneration policies need not be attached to the Board's Report
 - Policies to be made available on the website, if any, and web address to be indicated in the Board's report
 - Salient features of the policies and changes, if any, shall be specified in brief in the Board's report
- Abridged Board's report may be prescribed for one person company or small company
- With unnecessary attachments such as MGT9, CSR and Remuneration policies and certain disclosures, the Board's Report has become very bulky and costly to publish. The amendments has concised the Report, without any kind of compromise as far as the disclosures are concerned

135 Corporate Social Responsibility - (not notified)

- The threshold limits ‘during any financial year’ shall be replaced by ‘the immediately preceding financial year’
 - during any financial year could be interpreted as ‘any financial year during the life time of the company’.
 - now the limits are to be applied only in case of the previous financial year
- Where a company is not required to appoint independent director under section 149, it shall have the CSR committee with two or more directors
- CSR policy shall indicate the activities to be undertaken by the company **in areas or subject**, specified in schedule VII (broad areas)

Net Profit for the purpose of section 135

- CSR Rules define the term 'net profit'. However explanation to section 135(5) provides that for the purpose of this provision, the 'average net profit' shall be calculated in accordance with Section 198
 - As per this 'net profit' means net profit as per financial statement but shall not include any profit arising from any overseas branch or any dividend received from other companies which are covered under CSR
- Explanation: for the purpose of this section ~~Average Net profit shall not include such sums as may be prescribed~~ and shall be calculated in accordance with the provisions of section 198
 - This means that net profit for section 135(1) shall also be calculated in accordance with the provisions of section 198

136 Copies of audited financial statements

- The amendment act has aligned the dispatch of notice of AGM being conducted on shorter notice with the provisions of sending financial statements on shorter notice
- **Copy of the financial statements**, including consolidated financial statement **can be sent to members, less than 21 days before the meeting** if it is so agreed by members
 - If the company has share capital, majority in number entitled to vote and who represent not less than 95% of such part of the paid-up share capital of the company, as gives a right to vote at the meeting
 - If the company has no share capital, not less than 95% of the total voting power exercisable at the meeting
- This amendment takes care of holding AGMs at shorter notice under section 101 and sending financial statements also at a shorter notice
- Every listed company (earlier every company) having subsidiaries shall place separate audited accounts in respect of each subsidiary on its web site, if any

Financial statements of subsidiaries

- **Every listed company** which has subsidiaries incorporated outside India,
 - If such foreign subsidiaries statutorily required to consolidate, such consolidated financial statement shall be placed on its website
 - Where such foreign subsidiary is not required to get its accounts audited, such unaudited financial statement shall be placed on the website with a translated copy in English, if required
- **Every company (whether listed or unlisted)** having a subsidiary or subsidiaries shall provide a copy of separate audited or unaudited financial statements, as the case may be to any member of the company who asks for it
 - Though consolidated foreign subsidiaries can be placed on website, separate financial statements are to be provided, if asked for

Miscellaneous provisions

- **Section 137** – in case of a foreign subsidiary which is not required to get its financial statement audited, such unaudited statement shall be filed with ROC, translated in English, along with a declaration to this effect

AUDIT & AUDITORS

139 Appointment of Auditors

- First proviso relating to **ratification of auditors is removed**
- In case the shareholders decided not to ratify the appointment, the same amounts to removal of auditors
- Removal requires a special resolution and approval of Central Government, where as in case of non-ratification requires a simple resolution.
- However explanation to Rule 3 of Companies (Audit and Auditors) Rules, 2014 provides that in case the appointment is not ratified by the members, the Board shall appoint another Auditor after following the procedure
- *This anomaly is removed with this amendment*

141 Qualification of Auditors

- Sub-section (i) was amended as under:
- A person who, directly or indirectly renders any service referred to in section 144 to the company or its holding company or its subsidiary company
- **The above person shall not be eligible for appointment as an auditor of the company**
- For the purpose of this clause directly or indirectly shall have the same meaning assigned to it in the explanation to section 144

143 powers & duties of Auditors

- The auditors of the company which is the holding company shall also have the right of access to
 - the records of all its subsidiaries and associates in so far as it relates to the consolidation of its financial statements of the company with that of its subsidiaries and associates
 - Earlier they had right of access only to the records of subsidiaries only
- The auditors report shall state as per sub-section (3) (i) whether the company has adequate **internal financial controls system** in place and the operating effectiveness of such controls
 - the word internal financial controls system have been replaced with internal financial controls with reference to financial statements

147 punishment for contravention

- certain amendments have been proposed in the penal provisions for contravention of provisions relating to auditors
 - **In case of criminal liability** of an audit firm, concerned partner or partners, who acted in fraudulent manner or abetted or colluded in any fraud shall only be liable
 - **In case of civil liability** of the audit firm, partners will be jointly and severally liable

DIRECTORS

149 Independent Director

- Every company shall have at least one director who stays in India for a total period of not less than one hundred and eighty two days **during the financial year**
 - **earlier** the director was to stay for 182 days in the **previous calendar year**.
- In case of **newly incorporated company the requirement shall apply proportionately** at the end of the financial year in which it was incorporated
- *This enables the company to find a director who is staying and working for the company*

Pecuniary relationship in case of IDs

- **Pecuniary relationship**, other than remuneration as such director or having transaction not exceeding ten per cent of his total income or such amount as may be prescribed
- **Pecuniary relationship of relatives** of such director with the company, its holding, subsidiary or associate company have been elaborated in terms of shareholding, indebtedness, financial transactions etc
- In case of a relative who is an employee of the company, its holding, subsidiary or associate company, the restriction that not to be employed in any of the three financial years immediately preceding the financial year is not applicable

160 Right of person to stand for Directorship

- This section facilitates a person who is not a retiring director to be appointed as a director
- A notice together with a deposit of Rs one lakh proposing the name of such person for directorship shall be given to the company
- Now **the requirement of such deposit shall not apply in the following cases**
 - Appointment of an independent director
 - Director recommended by NRC, if any
 - Director recommended by the Board of Directors of the company where NRC is not required to constitute

161 Alternate Director

- Board may appoint a person not being a person holding any alternate directorship for any other director in the company or holding directorship in the same company
 - earlier a director company would have been appointed as an alternate director for other director, which is not permitted now
- A person can't be a director, as well as an alternate director for someone else at the same time

161 Casual vacancy

- Casual vacancy shall be filled by the Board at a meeting of the Board
 - Earlier this was applicable only for public companies
- Casual vacancy be filled by the Board at a meeting, which shall subsequently approved by members in the immediate next general meeting
- Earlier such approval was not required

164 Disqualification of Director

- A person who is appointed as a director of a company which is in default for non-filing of financial statement or annual returns or has failed to repay the deposits, interest etc. with the amendment, he
 - shall not incur the disqualification for a period of six months from the date of his appointment
 - Time permitted to the new director to make the company compliant
- Disqualification under sub-sections (1) (d), (e) and (g), **shall continue to apply even if the appeal or petition has been filed against the order of conviction or disqualification**
 - earlier this was not so and a time period was given

165 Number of Directorships

- For reckoning the **limit of directorships** of twenty companies, the **directorship in a dormant company shall not be included**

167 vacation of office of director

- Where a director incurs a disqualification for non-filing of annual returns or financial statements or failure to repay deposits, interest etc
 - the office of the director shall become vacant in all the companies other than the company which is in default under section 164(2)
- In case any director is disqualified by an order of court or Tribunal, or convicted of any offence, the office shall not be vacated
 - for thirty days from the date of conviction or order of disqualification
 - where an appeal or petition is preferred within thirty days, until expiry of seven days from the date of disposal
 - where in further appeal was preferred within seven days, until the same is disposed of

168 Resignation of Directors

- A director is **not under mandatory obligation to forward a copy of his resignation along with detailed reasons for his resignation to ROC**
- The intimation of reasons for resignation is made optional

MEETINGS

173 Meetings of Board

- Where there is a quorum in a meeting through physical presence of directors, any other director may participate through VC or other audio visual means on any matter
- This means that even the matters which can't be dealt with in a meeting through video conferencing or other audio visual means, can be dealt through VC now, provided that physical quorum is available
- *This is a welcome feature*

177 Audit Committee

- Every listed public company shall constitute an audit committee
 - earlier this was every listed company i.e. even a private limited company which has listed its debentures was to constitute AC
- Proviso to 4(iv) –where the audit committee does not approve the transactions, other than transactions referred to in section 188, (i.e. transactions not covered under section 188), it shall make its recommendation to the Board
 - earlier audit committee only has to approve the transaction and there was no recommendation to the Board.
 - as per this amendment if audit committee does not approve any financial transaction, it shall recommend it to the Board

177 Audit Committee contd.....

- Second proviso –
 - any transaction, not exceeding one crore rupees entered into by a director or officer of the company
 - without obtaining the approval of the audit committee and not ratified by the audit committee within three months
 - shall be voidable at the option of the audit committee
 - if the transaction is with a related party to any director or authorised by any other director
 - the director concerned shall indemnify the company against any loss incurred by it
- Third proviso
 - this clause shall not apply to a transactions between a holding company and its Wholly Owned Subsidiary, unless such transactions are referred to in section 188,

178 NRC & SRC

- Every listed public company shall constitute an NRC and SRC committees
- NRC shall specify the manner for effective evaluation of performance of the Board, its committees and individual directors to be carried out either by the Board, by the NRC or by an independent external agency and review its implementation and compliance
 - earlier NRC was to simply carry out the evaluation of every director's performance
- Remuneration policy shall be placed on the website of the company, if any, and the salient features of the policy and changes therein, shall be disclosed in the Board's report
 - Policy need not be attached to the Board's report

184 Disclosure of Interest

- Nothing in this section shall apply to
 - any contract or arrangement entered into or to be entered into between two companies or between one or more companies and one or more bodies corporate where
 - any of the directors of the one company or body corporate or two or more of them together holds or hold not more than two per cent of the paid-up share capital in the other company or the body corporate

LOANS TO DIRECTORS

185 Loan to Directors

- Unlike Section 295 of Companies Act, 1956 Section 185 is applicable to both Private and Public companies
- **This section virtually prohibits** making loans either **directly or indirectly**, giving guarantees or providing securities, by a company to its directors or to any other person in whom such director is interested
- **There is no provision for Central Government** approval unlike section 295
- The **objective of this prohibition** is **to prevent Directors from abusing their position of trust** to grant loans to themselves or to persons in whom they are interested, at the cost of the company
- Companies (Amendment) Act, 2017 completely rehashed this section

What is a Loan?

- Loan is not defined under the Companies Act
- According to Black's Law dictionary 'loan' means
 - Lending or advancing **money** with absolute promise to repay
 - A borrowing with a **promise to repay**
 - **Delivery of money** by one party and **receipt of money** by another on agreement express or implied
- Indirect Loan means
 - Loan through one or more intermediaries
 - By way of an accommodation

Loan transactions

- To attract section 185 there must be a transaction of a loan and it is **to be so intended and understood by both parties**
- **Terms of loan are to be decided** and accepted by both parties
- **Payment of advance** for supply of goods, or against purchase of a property or for services to be rendered, it **can't be treated as a loan**
- The above does not fall in 'indirect loans'
- A debt which is not in the nature of a loan can't be subsequently converted into a loan

Companies (Amendment) Act, 2017

- Companies (Amendment) Act, 2017 **substituted entire section 185** and has **substantially liberalised**
- Granting of loan, giving guarantee or providing security may be categorized as Prohibited, Conditional and Exempted
 - Assistance for some was **completely prohibited**
 - Assistance for some was **conditionally made possible**
 - Some **exempted categories** to whom assistance may be given without any restrictions

Complete Prohibition

- Section 185 (1) provides for complete ban on **advancing any loan** directly or indirectly, including any **loan represented by a book debt**, providing any **guarantee or security in connection with a loan taken** by
 - any director of the company,
 - any director of its holding company (subsidiary, Joint venture and associate companies directors are not covered);
 - any partner of the director of the Company or of the holding company;
 - any relative of the director of the company or of the holding company;
 - any firm in which any such director or relative is a partner
- In above cases its absolute prohibition and no provision for Central Government approval, unlike section 295
- **Section 185(1) stipulated restrictions only in respect of Individuals** and not of companies or body corporates

Conditional assistance

- Advancing loan, including loan represented by a book debt, providing guarantee or security in relation to any loans to ‘the **persons in whom the director is interested**’ is now permitted subject to the condition that -
 - the approval of members obtained by **special resolution** in general meeting
 - (this should be a prior approval. Advancement of loan is subject to the condition)
 - **disclosure in explanatory statement** full particulars and the purpose for which the loan, guarantee or security is **proposed to be utilised** by the recipient
 - **loans are utilised by the borrowing companies** for its principal business activities

Any person in whom Director is interested

- **Any person in whom Director is interested means –**
 - Any private company of which any such director is a director or member
 - This means common director / membership is not applicable to public companies. Hence public companies are not covered
 - **Any body corporate** at a general meeting of which **not less than twenty-five percent** of the total voting power may be exercised or controlled by any such director or by two or more such directors together or
 - Here public companies are covered provided the Director(s) hold or control not less than 25% of the voting power
 - Voting power held by the lending company is immaterial
 - **Any body corporate**, the board of directors, managing director or manager whereof is **accustomed to act** in accordance with the directions or instructions of the Board or of any director or directors of the lending company

Difficulties arisen on 'accustomed to act'

- Whether a **relationship as that of holding-sub subsidiary** between two companies would necessarily and always mean that subsidiary company is **accustomed to act** as per the instructions of the holding company?
- If so, **all holding companies are prohibited to lend money to its subsidiaries**
- **In section 295** loans made, guarantees given or securities provided by a holding company to its subsidiary **were exempted**
- No such exemption was provided in 185

Accustomed to act

- **Accustomed to act indicates** that there must be a regular or usual practice of issuing directions or instructions by the board or a director of one company to the other
- **“Accustomed to”** means customary, usual, habitual, habituated, acclimated be used to, being in the habit or custom
- Mere holding-subsidiary relationship between two companies will not *ipso-facto* establish that one is accustomed to act as per the instruction of the other
- **There should be instances or documents indicating advice, directions or instructions** by a director or manager of a company to the board, managing director or manager of the body corporate
- The board, manager or directors of the body corporate **act in accordance** with such advice, directions or instructions
- Hence it is **to be established that there have been series of events** in which they were accustomed to act and a **single isolated event or two would not be sufficient**
- There **must be an evidence and not based on presumption**

Exempted categories

- **Loan to Managing Director or Whole-time Director** –
 - as a part of service conditions extended to all its employees or
 - pursuant to a scheme approved by members by special resolution
- **Loan given** by the company **in the ordinary course of business**
 - Bank rate of interest has been replaced with yield of one year, three year, five year and ten year on Government security
- Loan given, guarantee or security provided by a **holding company to its wholly owned subsidiary company**
- Any guarantee or security provided by a **holding company** in respect of a loan provided by a bank or financial institution **to its subsidiary**
- Provided the **subsidiaries utilise the funds for its principal business activities**
- *The relaxation given goes a long way in ease of doing business, since the amendments eased the genuine difficulties faced by businesses in structuring their financial arrangements*

Some FAQs

- Whether Lender Company can give guarantee / Security to Subsidiary Company when loan taken from **other than** Bank and financial Institution?
 - The exemption provided in the Act is only Guarantee or security in respect of a loan made any bank or FI to its subsidiary. Hence such exemption is not available to loans taken from others
- Public companies per se does not fall under “persons in whom the director is interested”, then why under sub-section 3 **full exemption to WOS and partial exemption to subsidiaries** is given?
 - WOS and subsidiaries are presumed to be ‘accustomed to act as per the instructions’. Hence full exemption to WOS and partial exemption to subsidiaries is given.
 - If both companies are public companies with no common directors or members, then they have to establish that they are not accustomed to act as per the instruction of the lending company

Penal provisions

- Earlier if any loan is advanced or a guarantee is given or security is provided in contravention of the provisions, it was a punishable offence.
- Under the amended provisions ‘**the loan advanced is utilised in contravention**’ of the provisions is also a punishable offence
- Every officer of the company who is in default shall be punishable with imprisonment or with fine
 - earlier only the company, the Director and the recipient were liable

LOANS & INVESTMENTS

186 Loans & Investments

- Person does not include any individual who is in the employment of the company – hence interest free loans possible
- Aggregate of the loans and investments so far made, guarantees or securities so far provided along with the investment, loan, guarantee or security proposed, exceed the limits, it requires prior approval by way of a special resolution
- Prior approval by a special resolution in general meeting is not required for (substitution of sub-sec 3)
 - Loans or guarantee or security to WOS / Joint Venture company
 - Acquisition by holding company in WOS
- Company shall disclose details of the above in the financial statement

Exemption from 186 – (sub-section 11)

- Non-applicability of section 186 to ‘investments made by’
 - Banking companies, insurance companies, housing finance companies, companies with object of financing industrial enterprises or providing infrastructural facilities (Earlier this was available only for loans made or guarantees or securities provided)
 - Investment companies
- Investments made by body corporates in shares allotted on rights issues
- to lending activities by a non-banking financial company registered under chapter IIB of RBI Act, whose principal business is acquisition of securities
 - Earlier this was available only for acquisition of securities
 - Providing guarantees or securities by these companies still have to comply with provisions of section 186

188 Related party Transactions

- As per the second proviso **Related parties shall not vote on the 'ordinary resolution'** approving the related party transaction. This proviso **shall not be applicable to**
 - a company in which 90% or more members, in number, are relatives of promoters or are related parties (insertion of new proviso after second proviso)
- Non-ratification of transaction by the Board or Shareholders, shall be **voidable at the option of not only of the board but also of shareholders**
 - Earlier this option was only with the Board and now extended to shareholders also

MANGERIAL REMUNERATION

196 Appointment of MD / WTD / Manager (not notified)

- Where for appointment of managerial person, who has attained the age of seventy years
 - special resolution was not passed, but
 - votes casted in favour are in excess of votes casted against
 - with the approval of Central Government such appointment may be made (new proviso to sub-sec 3(a))

197 Managerial Remuneration - (not notified)

- For payment of remuneration exceeding 11%, subject to Schedule V, approval of **Central Government is removed** i.e. not required
 - Shareholders approval is required which should be subject to the provisions of Schedule V. “Ordinary Resolution is sufficient
- For payment exceeding the 5%, 10%, 1% and 3% limits approval of shareholders is required by way of **“Special Resolution”**

Managerial Remuneration contd

- In case of **default in payment of dues to**
 - **any bank or public financial institution** or non-convertible debenture holders or any other secured creditor
 - **prior approval of the concerned bank or public financial institution** or
 - **prior approval of the** non-convertible debenture holders or other secured creditor as the case may be
- shall be obtained before obtaining the shareholders approval
- If a company has no profits or inadequacy of profits and not complying provisions of Schedule V, **with the previous of Central Government is omitted.**
 - **This effectively means that companies with no profits or inadequacy of profits have to necessarily comply with the provisions of schedule V and can pay remuneration only as per schedule V**

Refund of excess remuneration paid

- When remuneration was paid in excess of limits, without the approval required,
 - the director shall refund the money within two years or such lesser period allowed by the company (sub-sec 9)
 - until such time, he shall hold the money in trust for the company
- Waiver of such refund is not permitted unless permitted by
 - Central Government is removed
 - substituted by approved by the company by special resolution within two years from the date the sum becomes refundable (sub-sec 10)
 - Insertion of new proviso – where the company has defaulted in payment of dues, prior approval of such institutions / creditors for such waiver before obtaining shareholders' approval

Insertion of new sub-sections

- In sub-section (11) also the approval of Central Government is removed
 - This effectively means that even if the articles or agreement provides for increase in remuneration if a company has not profits or inadequacy of profits, such company **can't pay remuneration beyond the limits of Schedule V**
- Auditor in his report shall make a statement that 'remuneration was paid in accordance with the provisions of this section'
 - Whether remuneration was paid in excess of the limits laid down and to give such other details as prescribed (new sub-sec 16)
- **Applications pending with Central Government shall abate** and company shall **within one year obtain approval** of shareholders (new sub-sec 17)
- *Discretionary powers of Central Government for approvals removed*

198 calculation of profits - (not notified)

- While calculating net profits, any amount representing unrealised gains, notional gains or revaluation of assets have to be excluded
- Amount representing profits by way of premium on shares or debentures of the company which are issued or sold by an investment company shall be allowed as credit to the P&L account

247 valuation by registered valuers

- Registered valuers shall not undertake valuation of any assets in which he has a direct or indirect interest or becomes interested **at any time** during or after the valuation of assets
- In the proposed amendment “at any time” has been amended “during the period of three years prior or after
- *Earlier it was a virtual ban and a relief has been given*

403 Fee for late filing - (not notified)

- Annual return and financial statements may be submitted after the period provided in the respective sections, on payment of additional fee of minimum Rs 100 per day and different amounts may be prescribed for different classes of companies
- For delay in filing documents other than annual return and financial statement prescribed additional fee is applicable
- **Default in two or more occasions** relating to late filings – attract payment of higher prescribed fees. Such higher fee shall not be less than twice the additional fee provided
- If the company defaults with regard to the above filings **the company and the officers of the company in default** shall, without prejudice to the liability of payment of fees and additional fee, be liable for the penalty or punishment provided under this Act
- *Penal provisions have been made very stringent*

447 Punishment for Fraud

- With the amendment Frauds which involve an amount of Rs 10 lakh or more or one per cent of the turnover of the company, whichever is lower, would be considered punishable under section 447
 - these frauds shall be punishable with imprisonment which shall not be less than six months but which may extend to ten years **and** shall also be liable to fine which shall not be less than the amount involved in the fraud but which may extend to three times the amount involved in the fraud (no change in this)
- As per the new proviso **frauds less than the above limits and not involve public interest**, would be punishable with an imprisonment for a term which could extend to five years **or** with fine which may extend to Rs 20 lakhs or with both
- First category of frauds are not compoundable whereas the second category of frauds are compoundable
- *Based on materiality penal provisions have been rationalised*



THANK YOU

S.SUDHAKAR VICE-PRESIDENT (CORPORATE SECRETARIAL),
RELIANCE INDUSTRIES LIMITED