



amarchand mangaldas

Companies Act, 2013

Key Highlights

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Implementation of the Companies Act 2013 (the “Act”)

Implementation Status

- On August 30, 2013, after having passed by the both houses of the Indian Parliament and receipt of assent of the President of India, **the Act has been notified** - It is subject to further notifications by the MCA to make it effective, and various provisions thereof have been made subject to corresponding rules
- A majority of the provisions of the New Act (*i.e.* **approx. 74%**) give power to MCA to make rules
- The New Act is divided into **29 chapters**, and contains **470 Sections** and **7 schedules**. 33 new definitions have been introduced in the New Act, *inter alia* including, Associate Company, Promoter, One Person Company, Independent Director, Key Managerial Personnel, Related Party *etc.*

Provisions Notified by MCA

- **283 provisions of the Act have been brought into force** – the provisions not yet into force primarily relate to compromises, arrangements and amalgamations, oppression and mismanagement, sick companies, winding-up and NCLT
- Rules corresponding to the notified sections have also been published – Rules for **19 chapters have come into effect from April 1, 2014**, and balance will come into effect from the date of publication in the official gazette



Related Party Transactions

Related Party Transactions

Related Party Definition (with reference to a Company)

- a director or his relative
- a key managerial personnel or his relative
- a firm, in which a director, manager or his relative is a partner
- a private company in which a director or manager is a member or director
- a public company in which a director or manager is a director or holds along with his relatives, more than 2% of its paid-up share capital
- any body corporate whose Board of Directors, managing director or manager is *accustomed to act* in accordance with the advice, directions or instructions of a director or manager (not including advice, directions or instructions given in a professional capacity)
- any person on whose advice, directions or instructions a director or manager is *accustomed to act* (not including advice, directions or instructions given in a professional capacity)
- any company which is:
 - a holding, subsidiary or an associate company of such company
 - a subsidiary of a holding company to which it is also a subsidiary
- a director or key managerial personnel of the holding company or his relative

Relative Definition

- members of a Hindu Undivided Family
- Husband / Wife
- Father / Mother (including step father and step mother)
- Son / Daughter (including step son and step daughter)
- Daughter's husband
- Brother / Sister (including step brother and step sister)

Related Party Transactions

Approval Requirements

- Audit Committee approval - for **ALL** related party transactions (including subsequent modifications)
- **Board** approval, at a meeting of Board, for **entering into the following RPTs**:
 - sale, purchase or supply of any goods or materials
 - selling or otherwise disposing of, or buying, property of any kind
 - leasing of property of any kind
 - availing or rendering of any services
 - appointment of any agent for purchase or sale of goods, materials, services or property
 - such related party's appointment to any office or place of profit in the company, its subsidiary company or associate company
 - underwriting the subscription of any securities or derivatives thereof, of the company
- Prior approval of **shareholders** by way of a **special resolution** required (with the related party shareholders not being permitted to exercise voting rights):
 - For entering into any contract / arrangement with a related party - in case of a company having **paid-up share capital of INR 10 Crores or more**
 - For entering into transactions exceeding prescribed thresholds – **for all companies**
- **Exception**: RPTs in '**ordinary course of business**' **AND** on '**arm's length basis**'. While, 'Arm's Length Transaction' is defined to mean a **transaction between 2 related parties** conducted as if they were **unrelated**, so that there is **no conflict of interest**, the expression 'Ordinary Course of Business' has not been defined

Related Party Transactions

Reporting

- Every such contact or arrangement to be referred to in the report of board of directors along with the justification

Conditions prescribed under the rules

- The agenda of the board meeting to provide prescribed information regarding the contract / arrangement – including details of factors *not considered* – along with rationale for not considering those factors
- Interested director not permitted to be present at the board meeting wherein the contract / arrangement is being discussed
- In the case of contract between holding company and wholly owned subsidiary – special resolution by the holding sufficient

In case of Breach

- If board / shareholder consent not obtained, as per the requirements, the contract or arrangement shall be **voidable at the option of the Board** and if the contract or arrangement is with a related party to any director, or is authorised by any other director, **the directors concerned shall indemnify the company against any loss incurred by it**
- Penalty (for unlisted companies) Fine not less than INR 25,000, but which may extend to INR 500,000
- Disqualification for appointment as director under Section 164(1)(g)



Loans, Guarantees, Investments *etc.*

Loans & Guarantees to Directors and Interested Persons

Loan etc. to
directors
or persons
in whom
directors are
Interested
(Section 185)

- The Act puts restrictions on advancing any loan, or give guarantee or security, to, or in connection with, *any director or any other person in whom the director is interested*, except if:
 - Loan to a MD or a whole time director pursuant to a **scheme approved by shareholders**
 - Loan to a MD or a whole time director as a part of conditions of service extended to employees
 - Company provides loans or gives guarantees or securities, in its ordinary course of business & interest is charged at a rate not less than the bank rate declared by RBI
- ‘Any other person in whom the director is interested’ been defined to mean:
 - A director of the lending company, or of a company which is its holding company or any partner or relative of any such director
 - Any firm in which any such director or relative is a partner
 - Any private company of which any such director is a director or member
 - Any body corporate at a general meeting of which not less than 25% of the total voting power may be exercised or controlled by such director, or by 2 or more such directors, together
 - 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
- **Exemptions:**
 - Any loan made by a **holding company to its wholly owned subsidiary company** or any guarantee given or security provided by a holding company in respect of any loan made to its wholly owned subsidiary company
 - Guarantee given or security provided by a holding company in respect of loan made by any bank or financial institution to its subsidiary company – **Does not cover loan**
 - Loans have to be utilized by subsidiary for its principle business activities

Loans & Guarantees to Persons / Body Corporates

Loan *etc.*, to
other persons
& body
corporates
(Section 186)

- Prior approval of shareholders (by way of a special resolution) required for a company to directly or indirectly, give any loan, or provide guarantee or security in connection with a loan to any other **BODY CORPORATE** or **PERSON**, exceeding higher of:
 - 60% of its paid-up share capital, free reserves and securities premium account; or
 - 100% of its free reserves and securities premium account
- Free reserves defined to mean: reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend
- Detailed disclosure in the financial statements
- Approval of all directors present in the Board meeting
- Prior approval of public financial institution if a term loan is subsisting, and there is a default in repayment of such loan, or threshold (of 60%) being breached
- Rate of interest on loan not to be lower than prevailing yield of 1 year, 3 year, 5 year or 10 year government security closest to the tenure of the loan
- Particulars to be included in a statutory register
- A company in default in the repayment of any deposits or in payment of interest thereon, not permitted to give any loan or give any guarantee or provide any security or make an acquisition till such default is subsisting

Loans & Guarantees to Persons / Body Corporates

Exemptions (Section 186)

- No exemption *vis-à-vis* private companies
- Special resolution not required for the following categories of loan, security or guarantee:
 - by a company to its wholly owned subsidiary or a “joint venture company” (not specifically defined).
 - by a banking company or insurance company or housing finance company - in ordinary course of business
 - by a company in the business of financing of companies
 - by a company providing infrastructural facilities

Investments

Inter-corporate Investments (Section 186(1))

- Prior approval of shareholders (by way of a special resolution) required for a company to directly or indirectly, acquire securities of other body corporate, exceeding higher of:
 - 60% of its paid-up share capital, free reserves and securities premium account; or
 - 100% of its free reserves and securities premium account
- Detailed disclosure in the financial statements
- Approval of all directors present in the Board meeting
- Prior approval of public financial institution if a term loan is subsisting, and there is a default in repayment of such loan
- No exemption *vis-à-vis* private companies
- Special resolution not required in the following investments / acquisitions:
 - by a holding company, by way of subscription, purchase or otherwise of, the securities of its wholly owned subsidiary
 - by NBFC registered with RBI, whose principal business is acquisition of securities
 - by company whose principal business is acquisition of securities
 - pursuant to a rights issuance

Investments

Layering Restrictions

- Companies are, *unless otherwise prescribed*, prohibited from making investment **through more than 2 layers of investment companies**
- No specific clarification in the rules in this regard
- **Exceptions have been carved for:**
 - Acquiring **foreign existing structure** having more than 2 layers of investment subsidiaries as per the laws of such foreign country; or
 - A subsidiary company having any investment subsidiary for the purpose of meeting the requirements under any law or any rule/regulation framed under any law for the time being in force



Issue & Allotment of Securities

Issue & Allotment of Securities

Further issue of share capital

- Now applicable to both public and private companies
- Rights issue:
 - letter of offer specifying the number of shares
 - timeline for acceptance not less than 15 days and not more than 30 days
 - Right may be renounced by a person in favor of another
 - Board to dispose non accepted shares in “such manner which is not dis-advantageous to the shareholders and the company”
- Preferential issue of shares/other convertible requires compliance with prescribed conditions, including:
 - Authorization by articles of association
 - Board and shareholder's approvals
 - Securities allotted *via* preferential offer to be made fully paid up at the time of their allotment
 - Allotment of securities be completed within 12 months from the date of shareholders' approval
 - Issue price to be determined by registered valuer
- Preferential issue to also comply with the conditions laid down for private placement including time line for allotment of shares, refund of application money *etc.*

Shares with differential voting rights

- Provisions applicable to both public and private companies
- Issuance of shares with differential voting rights requires compliance with prescribed conditions, including:
 - shareholders' approval *vide* ordinary resolution
 - volume of shares with DVR to not exceed 26% of total post issue paid up equity share capital (including with shares with DVR issued at any point of time)
 - detailed disclosure in Board report
 - Per the explanation rules: “differential rights attached to such shares issued by any company under the provisions of the Companies Act, 1956, ***shall continue till such rights are converted with the differential rights*** in accordance with the provisions of the Companies Act, 2013”

Issue & Allotment of Securities

Preference shares

- Issuance of preference shares subject to compliance with prescribed conditions *inter alia*, including shareholders' approval via special resolution, no subsisting default in the redemption of preference shares issued before/under the Act, or in payment of dividend due on any preference shares *etc.*
- Companies engaged in the setting up of infrastructural projects (as defined under Schedule VI to the Act) permitted to issue preference shares for a period exceeding 20 years (but not exceeding 30 years) subject to annual redemption of a minimum of 10% from the 21st year onwards / earlier, at the option of preference shareholders
- Distinction between cumulative and non-cumulative preference shares for the purpose of voting rights has now been done away with

Bonus shares

- Requires compliance with prescribed conditions including:
 - Available sources being free reserves, securities premium account, and CRR account
 - Authorization by articles of association
 - Board and shareholders' approvals
 - No default in payment of interest or principal in respect of fixed deposits or debt securities
 - No default with respect to payment of statutory dues of employees (such as PF, gratuity *etc.*)
- Board decision (recommending bonus issue) once announced, shall not be withdrawn

Issue & Allotment of Securities

Private Placement

- Provisions applicable to both public and private companies
- All securities covered
- Conditions to make an offer (or invitation of offer) by way of Private Placement include:
 - The offer of securities or invitation to subscribe securities can be made to maximum 200 persons in a financial year (excluding qualified institutional buyers (as defined in the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009), and employees under a scheme of employees stock option) and on such conditions as may be prescribed
 - All the money payable towards the subscription of securities to be paid through cheque, demand draft or any other banking channels (but not by cash)
 - Offer to be made to such persons whose names are recorded by the company prior to the invitation to subscribe, and that such persons shall receive the offer by name, and that a complete record of such offers shall be kept by the company and a complete information about such offer shall be filed with the ROC within 30 days of circulation of offer letter
 - Allotment of securities has to be done within 60 days from the date of receipt of the application money, else such application money has to be refunded to the subscribers within in next 15 days; in case of failure pay interest @ 12% p.a.
 - The company offering securities shall not release any advertisements or utilize any media, marketing or distribution channels or agents to inform the public at large about such an offer

Issue & Allotment of Securities

Debenture issuance

- Board definition provided as to include any instrument evidencing a debt
- Per the rules, pledge excluded as admitted security for issuance of secured debentures
- Instruments like commercial papers appears to be included in the definition of debenture. Per the deposit rules, deposits exclude commercial papers

Issuance at discount

- Only permitted for issuance of sweat equity
- Impact may not be significant given that the existing limited use of such flexibility, which in any case requires prior approval of the company law board



Deposits

Deposits

Deposits

- Exempted deposits, *inter alia*, include:
 - Amount received from a director (at such time of receipt) – provided that the director furnishes to the company a declaration that amount being given is not out of funds acquired by borrowing or accepting loans or deposits from others
 - Amount received against issue of commercial paper or any other instrument issued in accordance with guidelines / notification issued by RBI
 - Amount received by company from any other company
 - Amount received towards subscription of securities, including share application money or advance towards allotment of securities pending allotment, so long as such amount is appropriated only against amount due on allotment of securities. **Provided that in case of no allotment, monies must be refunded within 15 days else such application money shall be treated as deposit**
 - Amount raised by issue of bonds or debentures secured by first charge of charge ranking *pari passu* with first charge on any asset (referred to Schedule III) excluding intangible assets, or bonds or debentures compulsarily convertible into shares within 5 years
- Exemptions from applicability of provisions:
 - Banking companies, NBFCs and Housing Finance Companies
 - Such other company as the Central Government may specify – no such companies specified so far

Deposits

Acceptance of Deposits

■ Deposits from members:

- Provisions applicable to both **public** and **private companies** for *inviting, accepting* or *renewing* deposits
- Approval of shareholders in a general meeting
- Issuance of circular to members providing prescribed financial details of the company, and filing the circular with RoC at least 30 days before issuance
- At least 15% of the deposit amount (maturing during a financial year and next financial year), to be kept in a scheduled bank in a separate bank account - deposit repayment reserve account
- Deposit repayment reserve account to be used only for repayment of deposits
- Maintenance of deposit insurance
- Unsecured deposits required to be so quoted in every circular, form, advertisement or in any document related to invitation or acceptance of deposits
- Every deposit accepted to be repaid with interest in accordance with agreed terms

■ Deposits from public:

- Eligible companies being **public companies** having net worth of INR 100 crores or more, or turnover of INR 500 crores, or more
- Same conditions as deposits from members
- Company required to obtain the rating (including its net-worth, liquidity and ability to pay its deposits on due date) from a recognized credit rating agency and rating to be obtained for every year during the tenure of deposits
- Within 30 days of acceptance - create a charge on its assets of an amount not less than the amount of deposits accepted in favor of the deposit holders

Deposits

Existing Deposits Under 1956 Act

- Per the section, Company to repay **within 1 year** from **commencement of the Act** or from the **date on which payments are due**, whichever is earlier - any unpaid amount of deposits or any interest due thereon
- Per the rules, repayment of such deposits & interest as per due date(s)



Revised position of Private Companies

Revised position of Private Companies

Provisions now applicable to private companies:

- Deposit rules in relation to deposits from members
- Requirements regarding related party transactions
- Provisions relating to giving / making: loans, investments, securities, guarantees *etc.*
- Layering restrictions
- Requirements *vis-à-vis* Rights Issue, Private Placement, Preferential Allotment
- Remuneration limits / conditions applicable of MD / WTD / Manager
- Restrictions regarding issuance of loans / guarantee / securities to or in favor of directors and other interested persons now applicable
- Corporate Social Responsibility (subject to meeting prescribed thresholds)
- Consolidation of accounts – financial statements to include cash flow statements
- Rotation of auditors (subject to meeting prescribed thresholds)
- Vigil Mechanism (subject to meeting prescribed thresholds)



THANK YOU