Important provisions of the New Companies Bill, 2012

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The New Companies Bill 2012 has been passed in Loksabha recently and is likely to be passed in Rajyasabha in the ensuing budget session with or without modifications. Thereafter the President may give his assent and after the notification in Official Gazette, the same or such of its provisions as may be notified will come into existence.

The New bill which is going to be the new Act for the corporate sector in India has made far-reaching changes in the existing law applicable to them. The present Act i.e. The Companies Act, 1956 has been in existence for almost 55 years and the corporate sector as well as the professionals associated with it have been accustomed to its provisions and functioning. Rather they have developed a typical mindset in relation to the same. Now with the new law coming into force in the next few months, it is necessary to prepare ourselves not only with the new provisions but also changing our mindset well in advance. Therefore although the new law has not come into force, the present article is written so that the process of change will start in the minds of the all concerned. Instead of going through all the changes in the law, only some of the important provisions are discussed here.

In the new law, there will be 470 sections instead of 658 in the existing Act. Further there will be 7 schedules instead of 15 at present. Apart from this the notable difference is that in the proposed Act, more weightage has been given to delegated legislation. The government has proposed to take authority in its hand in respect of more than 400 matters by framing the rules. This means this much substantial part of the law would be embodied in rules which are easier to change from time to time without going through the process of getting parliament nod.

Further, most of the privileges, concessions and or exemptions which were hitherto available to a private limited company under the existing Act have been proposed to be removed. e.g Rights issue, commencement of business, private placement of shares, acceptance of deposits from members, directors and their relatives etc. This means that in most of the provisions, they will be on par with public limited companies.

Another notable feature is that the concept of One Person Company is introduced where only one person can form a company. It will be a private company. It is mandatory to nominate another person (with his consent) who shall become member in case of original member's death or his incapacity to contract. Such other person can withdraw his name or the original member can change the nominee and appoint another person in his place. Less stringent

procedures will be applicable to such companies. The concept of small companies and dormant companies are also introduced. They will be entitled to certain concessions in procedural matters.

Now let us note some of the important provisions in the new bill. A few new definitions have been introduced like independent director, related party, interested director, promoter, key managerial person (KMP) etc while the definition of officer in default is widened. It includes a person who under the immediate authority of the Board or KMP is charged with any responsibility. The earlier provision that the person has given his consent is absent now. This means that Dy. or Asst Company secretary or some other officers would also be held liable for offences under the Act, if the Board designate them as such. And for this, their consent is not necessary. Further, the share transfer agents, merchant bankers and registrar are also included in respect of matters where they are concerned.

The term 'independent director' is defined. It is wider than the definition in the Listing agreement. Further, under listing agreement the nominee directors of financial institutions are regarded as independent directors whereas under the bill, they are not independent directors.

The term 'Promoter' is defined and he is made liable for certain offences whether he is a director or not.

One of the most important changes is the change in the definition of a private limited company. In private company's definition, the clause of prohibition of invitation or acceptance of deposits from persons other than directors, shareholders or their relatives is gone. But at the same time private companies are now allowed to accept deposits only from members and the basic conditions which are prescribed are same as those for a public company. Although we need to see rules as and when prescribed, private companies are now subject to more stringent conditions and compliances in respect of deposits. In the new bill, for acceptance of deposits from members, special provisions are introduced and even Registrar of Companies (ROC) need to be informed in prescribed manner. For the first time, the concept of secured deposits is introduced. In case of deposits held by the existing companies, they have to be repaid within the due date or one year from the commencement of the new Act, whichever is earlier. However, National Company Law Tribunal (Tribunal) has power to extend time for repayment of deposit on an application filed by the company. But the most important part is the penal provision made for failure to repay deposit within the due date or one year or within the extended time allowed by the Tribunal. The penalty for the Company is minimum Rs. 1 cr which may extend upto Rs. 10 cr and every officer who is in default may get imprisonment upto seven years or fine of minimum of Rs. 25 lakhs and maximum of Rs. 2 cr or both. The term deposit includes any receipt of money by way of deposit or loan or in any other form by the company but excludes such categories as may be prescribed. Provisions for

rating, deposit insurance might be there depending upon the rules as may be prescribed. I feel this one condition, subject to what will be contained in the Rules, will lead to numerous problems of cash flow as well dispute among the shareholders and what not.

Now the concept of commencement of business, which was hitherto applicable to a public company, is introduced for a private company as well. A declaration is required to be filed by each company that the subscribers have paid their subscription and the paid up share capital is not less than Rs. 1 lakh or Rs. 5 lakhs as the case may be and also file a verification of address of registered office. This verification of address is required to be filed within 30 days of the date of incorporation. The company should have a registered office within 15 days of the incorporation.

Clause 56 stipulates that the company is supposed to issue share certificates to subscribers to memorandum within two months of incorporation which casts a responsibility upon subscribers to make the payment for the shares subscribed by them within two months.

In the present Act, it is not necessary for a private company to issue shares on rights basis however in the present bill, even private companies have to issue further shares on rights basis. For issue of shares to non-members and non-employees, a special resolution is required to be passed and the price should be determined by a registered valuer subject to rules as may be prescribed. Of course they can issue shares on private placement basis after complying with the provisions therefor. Presently in case of private companies, the Board of Directors can issue shares at any time subject to articles of association, to any persons without any restrictions as to procedure. However, this liberty will go after the new bill becomes a law. Notable condition for private placement is that the subscription has to be compulsorily by cheque/dd or banking channel and not in cash. Elaborate procedure is prescribed for private placement to ensure that it is truly a private placement including recording names of the persons to whom offer is made and filing of particulars of such persons within 30 days of the offer with ROC. The Company has to allot shares within 60 days or refund it within next 15 days otherwise liable to pay interest at 12% pa. No such allotment can be made unless the previous allotment is completed or abandoned. Money received in such issue has to be kept in a separate bank account and can be used only on allotment or can be used for refund. Thus practice of accepting share application money and showing the same as pending allotment in accounts for years cannot continue.

Another notable feature is that penalty for offences under the new law have been enhanced to very high levels. e.g. Annual return should be filed within 60 days of the annual general meeting or the last day by which the annual general meeting should have been held or within 270 days with additional fee as may be

prescribed, otherwise a fine of minimum of Rs. 50000/- and maximum of Rs. 5 lakh is imposable on the company and the officer in default is also liable to pay the fine and or may be imprisoned. Since the rules for filing fee are not yet known, we do not know whether filing fees also would be increased. Further, not only the penalty has been enhanced special provisions for the enforcement and speedy disposal have been made. Special courts are proposed to be constituted for trying offences under the Act. They may try the offences having punishment of imprisonment not exceeding three years in a summary way. Apart from Registrar or a person authorised by the Central Government, even a shareholder is authorised to file a complaint before the court. It is also proposed to appoint adjudicating officers who will adjudicate penalty for default or offences under the Act.

The scope of and ambit of disclosures in Directors' Report is enhanced. Notable among them is the specified extract of annual return, the disclosures in respect of directors' and independent director's appointment, criteria etc., risk management policy, details of related party contracts and in case of a listed company or some public companies, a statement on formal annual evaluation by the Board of Directors of its own performance and that of its committees and individual directors. This is a welcome step. For the first time, the government is going beyond mere financial disclosures by giving importance to non-financial disclosures as well.

A new authority viz. National Financial Reporting Authority will be constituted for accounting and auditing standards. It will have powers for investigation against chartered accountants who are auditors of a company and punish them, if found guilty of professional misconduct. It will exercise these powers to the exclusion of Institute of Chartered Accountants of India. Statement of objects of the Bill says that quasi judicial powers are given to this Authority to ensure independent oversight over professionals.

Another important provision is in respect of corporate social responsibility. Every company having a net worth of Rs. 500 cr or more or turnover of Rs. 1000 cr or more or net profit of Rs. 5 cr or more shall constitute a Corporate Social Responsibility committee and spend at least 2% of its average net profits of the immediately preceding three years. The Committee should have minimum three directors out of which at least one should be independent director. However, it appears that there is some drafting error here. A private company (or even a One Person Company for that matter which will have only one Director) has only two directors and if it falls under any of the aforesaid conditions, it will have to constitute a committee. However since it has only two directors, it is not known how it will have a committee of three directors out of which at least one should be independent director.

There is now a restriction on the appointment of an Auditor for not more than consecutive six years (subject to ratification by the members at every annual

general meeting) in case of companies other than listed company or company belonging to such class as may be notified. The latter will have individual auditors for not more than one term of consecutive 5 years or a firm for not more than two terms of consecutive 5 years. It is further provided that thereafter such auditor or firm cannot be appointed for next five years as auditor of the said company. Members of the company may resolve for rotation of partners of the firm. Existing listed companies have been given three years' time to comply with this condition. Further, the number of audit assignment an auditor can take at a time is reduced to 20. The auditor is debarred from providing specified services like book keeping, internal audit, designing of financial information system, investment advisory or investment banking services etc.

Hitherto, only an auditor was required to file a form with ROC in respect of his appointment. Now for the first time, a notice is required to be filed by the company as well with the ROC for the appointment of an auditor within 15 days of the appointment. A long list of disqualifications of auditor i.e. persons who cannot be appointed as auditors is given.

In the new bill, stringent provisions for duties of auditor/cost auditor /company secretary in practice have been made. In fact, it has virtually become the responsibility of professionals to ensure compliance with the law by the corporates. If they come across any offence against the company by any officer involving fraud, they must report to Central Government otherwise they will have to pay the fine of minimum of Rs. 1 lakh but which may go up to Rs. 25 lakhs. Further in case of any offence by the partner, not only the partner of the firm, but the firm also is jointly and severally liable for civil as well as criminal liabilities.

As far as Directors are concerned, the new bill has modified quite a few provisions and introduced some new provisions. They are summarised below.

a) For a class of companies as may be prescribed, they should appoint at least one woman director. At least one director should have stayed in India for not less than 182 days.

b) For independent directors, criteria for independence have been prescribed. For appointment of independent director, the Board has to confirm that the said director fulfils the conditions for such appointment.

c) Unlike in the past, now the director of a private company also has to file his consent for appointment as director.

d) Maximum number of directorship including alternate directorship should not exceed twenty in which directorship of public companies should not be more than 10. A lot of ornamental/professional directors will have to resign from many companies.

e) If a director absents himself for one year even with obtaining leave of absence, he will vacate the office.

f) Loans to directors are subject to restrictions in case of both private and public companies. Earlier, there were no restrictions in case of private companies.

Now let us have a look at some other important provisions. In case of inter corporate loans and other loans it is now compulsory to charge interest at a rate which is not lower than the yield on Government security of the similar tenor. This will put restrictions on transfer of funds within the group companies as and when required by promoters.

In case of related party transactions in case of some companies having specified paid up capital or transactions specified certain limit, a special resolution is necessary and members who are related parties are debarred from voting.

A provision has been made to investigate the true ownership or control of a company. The Government can appoint inspectors to investigate. With this, the practice of dummy directors and shareholders will probably decline.

Fast track merger scheme for small companies or holding and subsidiary companies or such other companies as may be prescribed is proposed. Provisions for merger with foreign companies are also there.

Special provisions for revival and rehabilitation of sick companies are made in the Bill. Since the rate of revival under Sick Industrial Companies (special provisions) Act was not up to the mark, special provisions for revival and rehabilitation have been made under proposed Companies Act itself.

National Company Law Tribunal and National Company Law Appellate Tribunal are proposed to be constituted. As far as possible, they will try to dispose off the petition or appeal within three months. If it is not possible, they will record the reasons for it and then the president or chairperson of the respective authority may extend the time not exceeding ninety days. Earlier, in case of CLB such provision was not there.

It is proposed to form a Mediation and Conciliation Panel of experts. From this panel, one or more experts may be appointed and he/they would give their report on the matters referred to him/them.

Thus overall, the Government appears to be serious on compliance angle. At the same time, they have proposed various measures to facilitate mergers, revival or rehabilitation of sick companies, improvement in corporate governance, disclosures etc. as well as plugging the loopholes in existing law. But the flip side is that instead of government departments, the responsibility for compliance has been cast upon professionals. This will increase cost of compliance for

corporates. This will also result in increase in business for insurance companies as more and more corporates and professionals may opt for covering risk by way of insurance. The importance of professional institutes will be reduced to some extent as the power to punish professionals and ensure compliance is being vested in government or its agency. It is pertinent to note that the National Financial Reporting Authority will frame accounting and auditing standards. In view of compulsory repayment of deposits by the companies, unless exemption is granted to private companies, cash flow problems may arise for them and some cases may lead to disputes. There may be increase in litigations under company law for various violations like tax laws. Hence as I said earlier, it is now necessary to change our mindset first.