KEY HIGHLIGHTS OF THE COMPANIES ACT, 2013

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The Companies Act, 2013(the "Act"), after having been passed by both houses of Parliament, received the assent of President on August 30, 2013 and was published in the official gazette. The Act is divided into 29 chapters and contains 470 sections and 7 schedules. However, the Central Government is carrying out a stage-wise implementation of the Act. Currently, 283 provisions of the Act have been enacted and rules corresponding to these sections have been published. Rules for 19 chapters have been enforced as on 1st April 2014 and the remaining chapters will come into effect from the date of their publication in the official gazette.

New concepts of one person company, class action suits, corporate social responsibility (CSR) and enhanced corporate governance standards have been introduced under the Act.

Key Changes in the Act

1. Incorporation of Companies

(i) The Act has introduced the concept of One Person Company for the first time, which allows incorporation of a company with only one person as a member.

(ii) The maximum number of members of a private company has been increased to two hundred members.

(iii) The existing concept of a private company being a subsidiary of a foreign body corporate which is presently being regarded as a subsidiary of a public company has not been specifically dealt with under the Act.

(iv) The definition of the subsidiary company now includes the component of equity shares as well as convertible preference shares to determine whether it is a subsidiary of the holding company(i.e. if any company is holding more than 50 per cent of total equity shares plus convertible preference shares of another company,

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such company shall be considered as the holding company).

2. Share Capital

(i) A new provision has been stipulated regarding free transferability of shares of public company providing that a contract or arrangement between two or more persons in respect of transfer of shares shall now be enforceable. Hence, such contracts will be enforceable by the company, thereby removing the ambiguity in relation to enforceability of the contracts imposing restrictions on transfer of shares, in case of public companies.

(ii) A company can issue shares at a discount only in case of sweat equity shares.

(iii) A company can now issue preference shares in relation to infrastructure projects, for a period exceeding twenty years but not exceeding thirty years, subject to redemption of minimum 10 percent of such preference shares annually from 21st year onwards or earlier at the option of the preferential shareholders.

(iv) The provisions relating to further issuance of share capital including preferential issue and bonus issue are also made applicable to private companies.

(v) With a view to ensure more transparency and accountability on part of the companies, provisions for offer or invitation for subscription of securities on a private placement basis have now been specifically dealt with under the Act. Accordingly, the offer or invitation to subscribe to securities on private placement can be made to such number of persons not exceeding two hundred (excluding qualified institutional buyers and employees of the company being offered securities under a scheme of employees stock option*)* in a financial year and shall also satisfy such conditions (including the form and manner of private placement) as may be prescribed.

(vi) The Act has introduced prohibition on forward dealing and insider trading in company's securities and is applicable to both public and private companies.

3. Board of Directors

(i) Concept of Independent Director ("ID") has been introduced. Some of the important points relating to IDs are mentioned below:

- Listed companies shall have at least 1/3rd of the total number of directors as IDs and minimum 2 in case of unlisted public companies having (i) a minimum paid-

up share capital of INR 10 crore; or(ii) a minimum turnover of INR100 crore; or (iii) outstanding loans or borrowings exceeding INR 50 crore;

- In order to qualify as an ID, a person is required to satisfy prescribed prerequisites which are more stringent than those stipulated in Clause 49 of the listing agreement ("Clause 49");
- Nominee director cannot be regarded as an ID;
- Maximum term period of ID has been restricted to five years and subject to a maximum of 2 such terms;
- ID cannot be granted any stock options in companies. This appears to be in direct conflict with Clause 49 read with the applicable SEBI guidelines, pursuant to which independent directors may be granted stock options; and
- ID shall abide by the prescribed code of conduct, which appears to be quite onerous on the ID.

(ii) Duties of directors have been specifically provided, including, to act in good faith and in the best interest of the company, not to have any direct/indirect conflict of interest with the interest of the company and to exercise duties with diligence and reasonable care.

(iii) Every listed company and every other public company having paid-up capital of INR 10 crore or more is mandatorily required to appoint Key Managerial Personnel ("KMP") which includes MD, CEO, CS and CFO.

(iv) An ID and non-executive director (not being promoter or KMP) are made liable only in respect of such acts of omission/ commission by the company which had occurred with their knowledge, attributable through board processes, and with their consent or connivance or where they had not acted diligently.

(v) Every listed company and every other public company having paid-up capital of INR 100 crore or more or turnover of ₹300 crore or more is required to appoint at least one woman director on its board.

(vi) Appointment of at least one director resident in India, i.e. a director who has stayed in India for at least 182 days in the previous calendar year, is made mandatory for all companies.

(vii) Maximum number of directors in a company has been increased from twelve to

fifteen. Further, no Central Government approval is required to increase the maximum number of directors beyond fifteen. Shareholders of companies may do so by passing a special resolution.

(viii) Maximum number of directorships of an individual in public companies has been brought down to ten.

(ix) Provisions regarding convening and holding of board meetings through video conferencing or other audio visual means, have been specifically provided. However, certain matters such as approval of annual financial statements, Board's report, prospectus, matters relating to restructuring of company shall only be discussed at a physically convened board meeting.

(x) Minimum seven days advance notice is required for holding a board meeting. However, in order to transact any urgent business, a meeting may be called at shorter notice provided at least one ID, if any, shall be present at such meeting, failing which, decisions taken at such meeting shall be circulated to all directors and shall be final only upon ratification by at least one ID, if any.

4. Committees of Board of Directors (only for public companies)

(a) Audit Committee ("*AC*"): The board of directors of every listed company and unlisted public companies with (i) a minimum paid-up share capital of INR10 crore; or (ii) a minimum turnover of INR 100 crore; or (iii) outstanding loans or borrowings or debentures or deposits, exceeding INR 50 crore shall constitute an AC, which shall comprise of minimum of three directors with independent directors forming majority. Majority of members of AC, including its chairperson, are required to be able to read and understand the financial statement.

(b) Nomination and Remuneration Committee ("NRC"): The board of directors of every listed company and every unlisted public companies with (i) a minimum paid-up share capital of INR 10 crore; or (ii) a minimum turnover of INR 100 crore; or (iii) outstanding loans or borrowings or debentures or deposits, exceeding INR 50 crore (same as AC) shall constitute an NRC, which shall comprise of three or more non-executive directors out of which minimum one half shall be IDs. Further, the Chairperson of the company (*whether executive or non-executive*) may be appointed as a member of NRC; however, such Chairperson shall not chair NRC. NRC shall formulate the criteria for determining qualifications, positive attributes and independence of a director and recommend to the

board a policy, relating to the remuneration for the directors and KMP.

(c) Stakeholders Relationship Committee ("*SRC*"): Companies with more than one thousand shareholders, debenture-holders, deposit-holders and any other security holders at anytime during a financial year have to constitute a SRC to consider and resolve the grievances of security holders. SRC shall comprise of a non-executive chairperson and such other members as the board may decide.

5. Auditors and Accounts

(i) As per the Act, auditors are required to mandatorily rotate every five years.

(ii) The appointment of auditors shall be mandatorily ratified by members at every annual general meeting of the company.

(iii) The Act also imposes an added obligation on the auditors of the company to report to central government if they believe that any offence involving fraud has been committed by the officers or employees against the company, within sixty days of their knowledge of such an offence.

(iv) Auditors are prohibited from rendering specified services to the company/its holding company / subsidiary company, *inter-alia,* including:

- (a) internal audit;
- (b) investment banking services;
- (c) outsourced financial services;
- (d) actuarial services;
- (e) investment advisory services;
- (f) management services;
- (g) any other kind of services as may be prescribed.

(v) The Central Government is empowered to constitute, by notification, the National Financial Reporting Authority ("NFRA") to provide for matters relating to accounting and auditing standards. NFRA shall perform functions as specified, including monitoring the compliance and overseeing the quality of service of professionals associated with ensuring the compliance with such standards. Unlike the National Advisory Committee on Accounting Standards, the NFRA is not merely an advisory body. It has also been empowered to investigate, either *suo*

motu or on a reference made to it by the Central Government, into the matters of professional and other misconduct committed by any member of Institute of Chartered Accountants of India. NRFA has also been empowered to impose specified penalty including debarring the professional from the practice.

6. Corporate Social Responsibility ("CSR")

(i) CSR has been made mandatory for a company having net worth of INR 500 crore or more, or turnover of INR1,000 crore or more or a net profit of INR 5 crore or more during any financial year.

(ii) Such company is required to constitute a Corporate Social Responsibility Committee of the board ("CSRC") which shall consist of three or more directors. Except for private companies, in all other companies at least one director shall be an independent director.

(iii) SRC shall formulate and recommend to the board, a Corporate Social Responsibility Policy ("CSRP") indicating corporate social activities which include eradicating hunger and poverty, promoting education, gender equality, environment sustainability, protect national heritage and culture, contribution to PM Relief Fund and rural development projects to be undertaken by the company.

(iv) CSRC shall recommend to the board, the amount of expenditure to be incurred toward CSR and also monitor the same from time to time.

(v) Such company shall spend, in every financial year, at least 2 per cent of the average net profits of the company made during three immediately preceding financial years, in pursuance of its CSRP.

(vi) Such company shall also give preference to the local area(s) around it where it operates, for spending the amount earmarked by it for CSR activities.

(vii) In case of any failure on the part of the company in spending the aforesaid amount, the board shall give, in its report, the reasons for not spending aforesaid amount.

7. Serious Fraud Investigation Office ("SFIO")

(i) The Act has now established SFIO as a statutory body to investigate frauds relating to a company. This is an attempt to strengthen the already existing SFIO by empowering them with more powers and resources to expedite the investigation process.

(ii) Report of SFIO filed with the relevant court for framing charges shall be treated as

a report filed by a police officer.

(iii) SFIO is empowered to make arrest in respect of certain offences involving fraud.

(iv) The offences shall be cognizable and the accused person shall be released on bail only upon fulfilling the stipulated conditions.

8. Compromises, Arrangements and Amalgamations (provisions are yet to be notified)

(i) Under the Act, the merger of Indian companies with foreign companies incorporated in such countries as may be notified, has now been permitted.

(ii) Postal ballot has been added as a mode of voting on the scheme of compromise or arrangement.

(iii) Any objection to a scheme can be made only by persons holding not less than 10per cent of the shareholding or having outstanding debt amounting to not less than 5 per cent of the total outstanding debt.

(iv) In case of merger of a listed company with an unlisted company, the listed company is required to provide exit opportunity to its shareholders to opt out of the unlisted transferee company.

(v) An acquirer or a person acting in concert with the acquirer or a person / group of persons holding 90 per cent or more of the issued equity share capital of a company by virtue of an amalgamation, share exchange, conversion of securities or for any other reason, may now purchase the minority shareholding of the company at a price determined by a registered valuer in accordance with the rules prescribed.

(vi) Minority shareholders may also offer to the majority shareholders the shares held by them at a price determined by a registered valuer in accordance with the rules prescribed.

(vii) Merger between small companies or between a holding company and its wholly-owned subsidiary or such other classes of companies as may be prescribed, shall be approved by the Registrar of Companies and Official Liquidator without the requirement of obtaining National Company Law Tribunal's (NCLT) approval, subject to fulfilment of prescribed conditions.

(viii) Mandatory notification of the scheme shall be made to multiple regulatory authorities including the central government, income tax authorities, RBI, SEBI,

stock exchanges, CCI and other relevant sectoral regulators.

9. Winding up

The following new grounds for winding up by the NCLT have been inserted:

(a) the affairs of the company have been conducted in a fraudulent manner;

(b) the company was formed for fraudulent and unlawful purpose; and

(c) the persons concerned in its formation or management have been guilty of fraud, misfeasance or misconduct in connection therewith.

10. NCLT/NCLAT, Special Courts and Mediation and Conciliation Panel

(i) The provisions in respect composition and constitution of National Company Law Tribunal and National Company Law Appellate Tribunal have been redefined in view of the Supreme Court's judgment dated May 11, 2010.

(ii) For the speedy trial of offences, Central Government has been empowered to establish Special Courts in consultation with the Chief Justice of High Courts. Special Courts have liberty to try summary proceedings for offences punishable with imprisonment for a term not exceeding three years.

(iii) Central Government shall maintain the Mediation and Conciliation panel, which shall consist of such number of experts having such qualifications as may be prescribed. Such panel shall facilitate necessary arbitration between the parties during the pendency of any proceedings before the Central Government or NCLT or NCLAT.