COMPANY LAW – UNIT – II

Major principles – Nature and types of companies, Formation, Memorandum and Articles of Association, Prospectus, Power, duties and liabilities of Directors, winding up of companies, Corporate Governance, Amendment of Companies Act 2013.

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2.1 NATURE OF COMPANY

What is a company?

- A company is an artificial person created by law.
- A company means a group of persons associated together for the attainment of a common end, social or economic.

Definition of a company:

- According to Sec (1), "A company formed and registered under the act".
- According to Sec (3) of the act, "on incorporation a company becomes a body corporate or a corporation with a perpetual succession and a common seal."

Separate legal entity:

- A company is a separate legal entity means it is different from its members. It works as an individual body.
- It can make contracts, open a bank account, can sue and be sued by others.
- The law has recognized that even if a person holds virtually all the shares, the right and obligations of the company shall be different from its members.

Artificial person:

- A company is a purely a creation of law. It is invisible, intangible and exists only in the eyes of law.
- It has no soul, no body, but has a position to enter or exit into a contract, to appoint a people as its employees.
- In short it can do everything just like a natural person.

Perpetual existence [sec 34(2)]:

- Section 34(2) of the act states that an incorporated company has perpetual life.
- The life of the company is not related to the life of the members. Law creates the company and law alone can dissolve it.
- The existence of the company is not affected by death, insolvency, retirement or transfer of shares of members.

Limited liability:

- It means that the liability of a member shall be limited to the value of the share held by him; he cannot be called upon to bear the loss from his personal property.

Common seal:

- A company being an artificial person cannot work as a natural being.
- Therefore, it has to work through its directors, officers and other employees. Common seal used as an official signature of a company.

Transferability of share sec (82):

- The shares of a company are freely transferable. The shareholder can transfer his share to any person without the consent of other members.

- A company cannot impose absolute restrictions on the rights of member to transfer their shares

2.2 TYPES OF COMPANIES

2.2.1 Classification on the basis of incorporation

1. **Statutory companies:**

   These are created by special act of the legislature.

   - E.g.: The Reserve bank of India
   - The Life Insurance corporation
   - The Unit Trust Of India

2. **Registered Companies:**

   These are the companies which are formed and registered under the companies Act, 1956 or were registered under any of the earlier companies act.

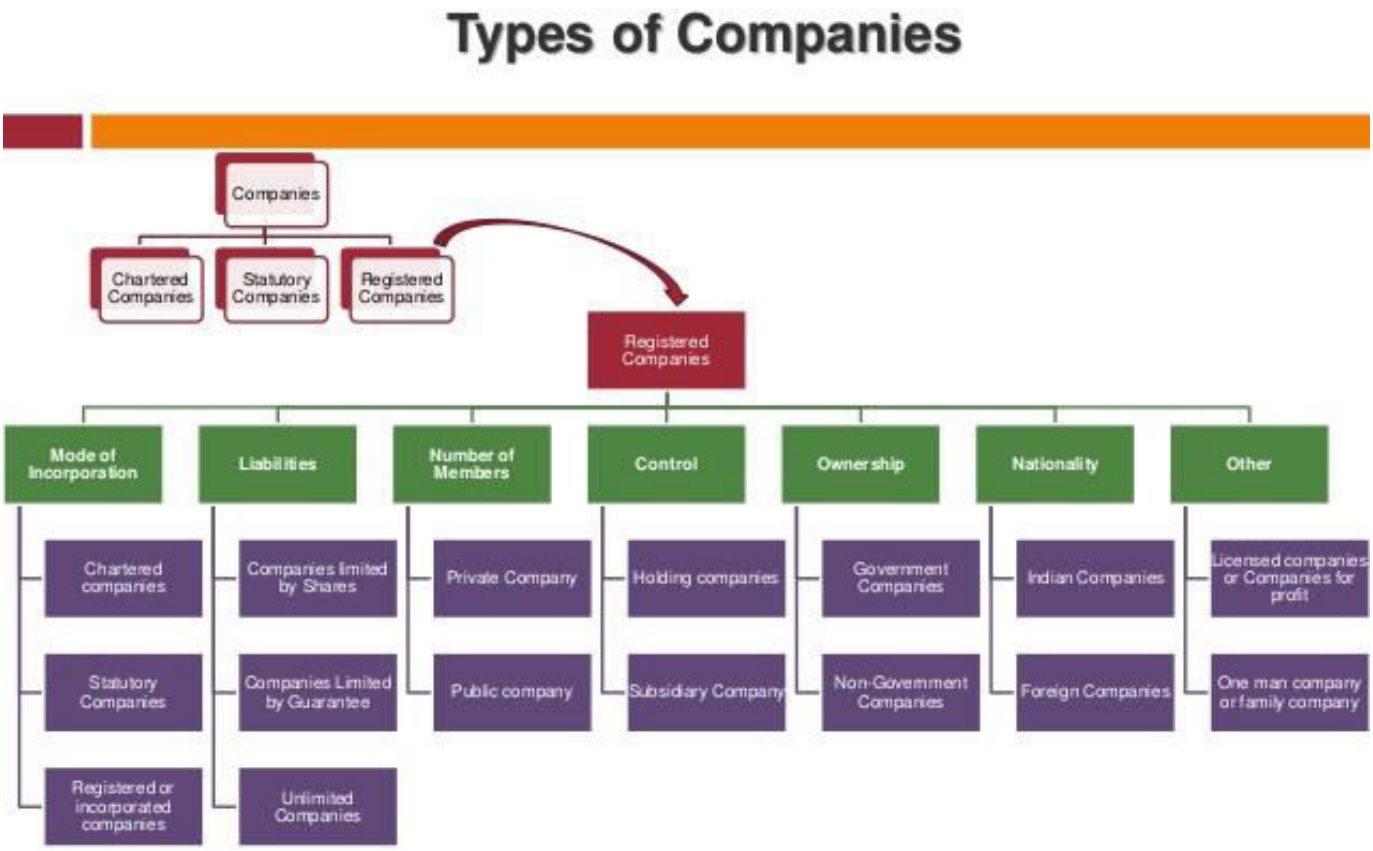
2.2.2 Classification on the basis of liability

1. **Companies with limited liability:**

   a. **Companies limited by shares**

Examples:

- Infrastructure Corporation of Andhra Pradesh Limited,
- MSEB Holding Company Limited,
- Maharashtra State Power Distribution Company Limited,
- Maharashtra State Power Generation Company Limited and
- Maharashtra State Power Transmission Company Limited.



b. Companies limited by guarantee

Examples

- Schools & Educational Establishments

- Clubs & Associations
- Charities and Organisation intending to apply for charitable status
- Churches & other Places of Worship
- Trade or Research Associations

2. Unlimited companies

Examples

- Jonathan Rose co.,
- Wicks Group of companies
- Suyog system and Software pvt. Ltd.

2.2.3 Classification on the basis of number of members

1. Private company

A private company means a company which has a minimum paid up capital of Rs.1,00,000 or such higher paid up capital as may be prescribed , and by articles –

a. Restricts the right to transfer its shares, if any. This restriction is meant to preserve the private character of the company.

b. Limits the number of its members to 50 not including its employee-members.

c. Prohibits any invitation to the public to subscribe for any shares in or debentures of the company.

d. Prohibits any invitation or acceptance of deposits from persons other than its members, directors and their relatives.

2. Public company

A public company means a company which

- Has a minimum paid up capital of Rs.5 lakh or such high paid-up capital, as may be prescribed.

2.2.4 Classification on the basis of control

1. **Holding company**

   A company is known as the holding company of another company if it has control over that other company.

2. **Subsidiary company**

   A company is known as a subsidiary of another company when control is exercised by the latter over the former called a subsidiary company.

   - Company controlling composition of Board of Directors.
   - Holding of majority of shares.
   - Subsidiary of another subsidiary.

2.2.5 Classification on the basis of ownership

1. **Government company**

   A Government Company means any company in which not less than 51% of the paid-up share capital is held by:

   - The central government or
   - Any state government or governments or
   - Partly by the central government and partly by one or more state governments.
     - E.g.: State Trading Corporation of India Limited.
     - Minerals and Metals Trading Corporation of India limited.

2. **Non-government company**

   Foreign companies.

2.3 FORMATION OF A COMPANY

2.3.1 Important Documents Before Approaching the Registrar

- An industrialist licence if the proposed business is covered by industries act 1951.

- An important licence is required if machinery is imported.
- Approval of govt. In case of foreign collaboration.
- Approval of govt. Under monopolies and restrictive trade practice act 1961, if necessary.

2.3.2 Documents Needed

- Memorandum of association
- Articles of association
- List of the directors
- Consent letter from directors
- Statement of capital
- Statutory declaration

2.4 MEMORANDUM OF ASSOCIATION

- It is an important document which defines objectives, powers, scopes and relations with outsiders.
- Some of the important clauses of memorandum of association are as follows:

1. **NAME CLAUSE:**
    - Company should not use any objectionable or identical names according to emblems and names act 1950.
    - The words "private limited" in case of private and "limited" in case of public company at the end.
    - Companies which are formed for the arts, culture, and commerce etc., the word "limited" are not needed.
2. **SITUATION CLAUSE:**
    - Every company will have registrar office.

- It is compulsory to mention the place and state of registrar office.
- If place is not confirmed, then it should communicate with the registrar within 30 days of its incorporation.

3. OBJECTIVE CLAUSE:

Here the company should mention its:

- Main Objectives
- Subsidiary Objectives
- Other Objectives

4. LIABILITY CLAUSE:

The extent and nature of the liability of shareholders should be stated like:

- Limited Liability
- Limited By Guarantee
- Unlimited

5. CAPITAL CLAUSE:

- Division of capital into shares of different dominations.
- The extent of each capital should be specified.
- The authorized capital should be mentioned.
- A company is not authorized to issue above authorized capital.

6. ASSOCIATION CLAUSE:

- This clause contains declaration of members.
- The names, addresses and occupations of the subscribers should be mentioned.
- The signatures are to be attested by proper witness.

2.4.1 Alteration of a Company

- With regard to changing the name,
  - Government permission
  - Special resolution
- In case of change in registrar office
  - Permission of the company law board is required.
- In case of change in objective clause
  - Special resolution with company law board permission.
- A copy should pass to the registrar within 30 days.
- In case of increase in capital – ordinary resolution and
- In case of decrease in capital – special resolution along with court permission is required.

2.5 ARTICLES OF ASSOCIATION

Certain rules and regulations that are necessary for the management of the company are listed in the articles of association. Every company has to prepare its own articles.

2.5.1 Contents of Articles of Association (AOA)

- Different kinds of shares to issue
- Mode of allotment of shares and calls on shares
- Procedure of issuing share certificates
- Procedure for transfer of shares and re-issue of shares
- Payment of commission on underwriting and brokerage on shares and debentures
- Declaration of dividend and issue of bonus
- Method to appropriation of profits
- Division, consolidation and re-organisation of share capital

- Rules for adoption of primary contracts
- Use of common seal
- Rules for conducting meetings
- Procedure for passing resolutions
- Method of accounting adopted by the company
- Method of maintaining bank accounts
- Winding procedure of the company etc.

2.5.2 Alteration of Articles of Association (AOA)

- Permission of court is not necessary.
- Special resolution and approval of government is required.
- But in some cases they should follow companies act as well as memorandum.

Other Documents:

List of Directors:

- The list of directors who have agreed to act as a directors should file with the registrar
- They should submit their:
    - Names
    - Age
    - Occupation
    - Full addresses
- In case when the list is not ready memorandum will be deemed to be the directors.

Consent Letter of Directors:

- Every person who is ready to act as director must give a written undertaking stating that he is willingly agreed to act as a directors of the company.
- Along with the letter the must subscribe the qualification of shares as mentioned in articles of association and have paid the amount accordingly.

Name Approval Certificate:

- A copy of letter from the registrar announcing that the name of company was approved without any objection.

Statement of Authorised Capital:

- The company should prepare and submit a statement of proposed capital which is authorized for collection from the public.
- It contains the number of shares and debentures and the amount of each category.

Statutory Declaration:

- A copy of statutory declaration should be enclosed stating to that all the formalities have duly compiled with as per the provisions of companies act.
- It should be signed by an advocate of High Court or the Supreme Court or a charted accountant or a director or a secretary or manager.

Receipt of Registration Fee:

- It is necessary to attach the receipt of the registration which is paid to registrar office of which it is calculated based on the authorized capital of the company.

2.5.3 Issue of Certificate of Incorporation

- After the receipt of all the documents, the registrar will scrutinize the documents.
- After everything is satisfied, the registrar will issue the certificate of incorporation.
- With this certificate, the company gets its recognition as a body of corporate.
- A private company can start its operations immediately after obtaining the certificate of incorporation.
- But a public company has to wait till it gets "certificate of commencement of business".
- This certificate should be obtained within one year of its incorporation failing which the court can pass an order for its closure.

2.6 PROSPECTUS

- "Prospectus" is the basic document for raising funds from the public.
- "Prospectus" refers to any document described or issued as prospectus and includes any notice, circular, advertisement inviting deposits or offers from the public for the subscription or purchasing of any shares, or debentures of the company.
- Thus prospectus is a general invitation to the public to subscribe to the capital of the company on the conditions specified in the application form.

2.7 POWER, DUTIES AND LIABILITIES OF DIRECTORS

Liabilities of Directors:

- Breach of duties
- Breach of accountability (section 213 & section 214)
- Reckless trading
- Prospectus liability
- Insolvency act(section 424)
- Personal liability company

Director Responsibilities:

Core Duties – Section 76

- Disclose any conflict of interest.
- Use position and information for company's benefit.
- Disclosure of material information.
- Perform duties:
  - In good faith
  - In best interest of the company
  - With care, skill and diligence

Strategy and Corporate Structure:

- Duty to comply with the act in relation to different types of companies (section 8).

- Duty to comply with the company's memorandum of incorporation (section 13).
- Duty to manage the business affairs at the company (Section 66(1)).
- Duty to carry on the business without trading recklessly or under insolvent conditions. (Section 22).

Board Structure and Corporate Administration

- Duty to appoint board committees (Section 72).
- Duty to appoint an audit committee (Section 94).
- Duty to appoint a company secretary (Section 84 & 86).
- Duty to call and convene a shareholder's meeting (Section 61).

Accountability and Assurance:

- Duty to keep company records (section 24).
- Duty to Keep Accounting Records (Section 28).
- Duty to comply with chapter 3 of the act (section 34(1) & 94).
- Duty to pay directors remuneration in terms of memorandum of incorporation and get it approved by shareholders by special resolution (section 66(8) & 66(9)).
- Duty to appoint auditors (section 90 & 92).
- Duty to obtain an independent review of the financial statements (section 30).

Disclosure and Transparency:

- Duty to prepare annual financial statements (Section 29 & 30).
- Duty to prepare a director's report (Section 30(3)).
- Duty to issue a prospectus (Section 100).
- Duty to disclose director's remuneration information (Section 30).
- Duty to file an annual return (Section 33).

Shareholder Treatment:

- Duty to ensure that shareholders can exercise their voting power and rights (section 2(2) & 58).
- Duty to facilitate a shareholders meeting (section 61).
- Duty to operate within the framework of the company's memorandum of incorporation (section 15(3) & (4) & 36).
- Duty to operate in the best interest of the shareholders (section 20(6) & (7) the company (section 76(3)).

2.8 WINDING UP OF COMPANIES

2.8.1 Winding Up

1. Winding up of a company is the process whereby its life has ended and its property administered for the benefit of its creditors and members.

2. Modes of Winding up - A company may be wound up in any one of the three ways:

   a. compulsory winding up i.e., by Court (section.433)
   b. voluntary winding up; (section.484)
   c. voluntary winding up subject to the supervision of the Court.(section.522)

2.8.2 Winding up by the Court / Compulsory Winding up

Section 433 provides that a company may be wound up by the Court:

1. If the company has, by special resolution, so resolved;

2. If default is made in delivering the statutory report to the Registrar or in holding the statutory meeting, where applicable; but petition should be filed within 14 days.

3. If the company within a year from its incorporation, or does not commence its business suspend its business for a whole year.

4. If the number of members is reduced
   - in the case of a public company, below 7, and
   - in the case or a private company, below 2;

5. If the company is unable to pay its debts(s.434)

6. If the Court is of the opinion that it is just and equitable that the company should be wound up.

A company shall be unable to pay its debts:

1. If a creditor to whom the company owes more than Rs. 500 then due, has served on the co. a demand in writing and the co. has within 3 weeks thereafter neglected to pay or secure or compound the sum to the reasonable satisfaction of the Creditor.

2. If an execution or other process issued on a decree or order of any court in favour of Creditor has not been satisfied by the Company.

3. If is proved to the satisfaction of the court that the company is unable to pay its debts including contingent and prospective liabilities.

A company can be wound up on "just and equitable" basis:

1. When there is a dead lock in the management.

2. When the company was found for fraudulent or illegal purposes.

3. When the principal shareholders have adopted an aggressive policy towards the minorities.

4. When the company is a "bubble".

5. When the business of the company carried except at loss.

6. When the private company is in essence or substance a Partnership.

7. Requirements for investigation.

2.8.3 Who can present petition for winding up?

1. By the company
2. By any Creditors
3. By any contributor
4. By the Register
5. By the central Government

2.8.4 Procedure for winding up

1. Date of commencement of winding up - date on which the petition is presented to court. As such, until winding up order is made, the company will have to comply with the requirements of the companies act as are required if company not wound up. However in case if voluntary winding up, the winding of the company is deemed to have commenced at the time of the passing of the resolution.

2. Hearing of Petition - notices issued to all concerned parties. Before hearing the petition the provisional liquidators are appointed to safe guard the assets of the company.

3. Intimation to Official Liquidator /ROC.

4. On hearing the petition the court may dismiss it, with or without costs.

5. Adjoin the hearing conditionally or unconditionally, make any interim order that it thinks fit, make an order for winding up the company with or without costs or any other order that it thinks fit.

Consequences of Winding up order:

1. The court must, as soon as the winding up order is made, cause intimation thereof to be sent to the official liquidator and the registrar (s.444).

2. The petitioner and the company must also file with the registrar within 30 days a certified copy of the order (s.445 (1)). In case the certified copy is not filed the petitioner is fined (s.445).

3. The registrar should take the minutes in his book and notify in the official Gazette that such order has been made(s.445(2)).

4. The order for winding up is deemed to be a notice of discharge to the officers and the employees except when the business is continued.

5. Suits against the company are stayed, unless the court gives leave to continue or commence proceedings.

6. All power of the board of directors cease and the same are then exercised by the liquidator (s.491, s.505).

7. On the commencement of the winding up the limitation ceases to run in favour of the company.

8. Any disposition of the property of the company and any transfer of shares in the company are then void. The official liquidator, by virtue of his office becomes the liquidator of the company and takes possession and control of the assets of the company (s.536 (2)).

9. Any distress or execution put in force without the court orders are void (s.537 (a)).

10. Any type of sale or floating charge created within the period of proceedings are void.[S534]

Statement of affairs to be made to the liquidator:

Order of Dissolution by the Court -thereafter the company has no existence.

Voluntary winding up:

Winding up by the members or creditors without any intervention of the Court is called voluntary winding up.

As per section 484, a company may be wound up voluntarily,

- By Ordinary resolution or by Special resolution.
- By passing an ordinary resolution in general meeting.

  a. Where either the time fixed by the articles for the duration of the company has expired OR
  b. The event specified in the Articles has occurred on which the company is to be dissolved.

In any other case, the company may resolve to be wound up voluntarily by passing a special resolution in general body meeting of shareholders.

A voluntary winding up is deemed to commence from the time the resolution for voluntary winding up is passed.

When the company has passed the resolution for voluntarily winding up, it must within 14 days, give notice in official gazette and also in some newspapers.

2.8.5 Consequences of Voluntary Winding-up

- A voluntary winding up is deemed to be commencing at the time when the resolution for voluntary winding up is passed.
- The company, from the commencement of the winding up, must cease to carry on its business except so far as may be required to secure a beneficial winding up.
- The transfer of shares and alterations in the status of members, made after commencement becomes void.
- A resolution to wind up voluntarily operates as notice of discharge to the employees of the company.
- On the appointment of the liquidator, all the powers of the board of directors shall cease except after the permission of the registrar.

2.8.6 Types of voluntary winding up

Types of Voluntary Winding up – Voluntary winding up may be of two types, namely,

1. Members' voluntary winding up

2. Creditors' voluntary winding up.

1. Members' Voluntary Winding up:

Members' voluntary winding up is possible only in case of solvent companies.

a. Declaration of Solvency (s.448)

- The directors must enquire whether the company will be able to pay all its debts within the period of 3 years.
- In order to be effective, this declaration must be made within 5 weeks immediately preceding the date of passing of the winding up resolution by the members;
- Delivered to the Registrar for filing;
- Must be accompanied by a copy of the report of the auditors of the company on the accounts and balance sheet.

b. Appointment and remuneration of liquidators: (s.492)

The company in general meeting must:

- appoint one or more liquidators
- fix the remuneration

Any remuneration so fixed cannot be increased in any circumstances whatever, whether with or without the sanction of the court. No liquidator shall charge of his office unless his remuneration is fixed.

c. Board's power to cease: (s.491)

- On the appointment of the liquidators all the powers of the directors cease but their powers may continue if the general body or the liquidator sanctions it.

d. Notice of the appointment of the liquidator to be given to the registrar (s.493):

- Within 10 days of his appointment, otherwise Rs.1000 fine per day.

e. Power of liquidator to accept shares, etc., as consideration of sales of property of the company (s.497)

f. Duty of liquidator to call creditors meeting in case of insolvency (s.495):

- If the liquidator finds that the company will not be able to pay its debts he should tell it to the creditors with all records.

g. Duty of liquidator to call general meeting at the end of each year (s.496):

- In case the winding takes more than one year the liquidator must call a general meeting and tell the acts and winding operations done by him.

h. Final meeting and dissolution(S497):

- The liquidator must make up an account of the winding up showing how the company has been disposed of. He must call the general meeting of the company for laying the account before it with explanations.

2. Creditors Voluntary Winding Up:

Creditors' voluntary winding up – Where the Board of directors does not file a declaration as to solvency of the company, the voluntary winding up is called „ the Creditors „ voluntary winding up.

- If the members and creditors nominate two different persons as liquidators, creditors' nominee shall become the liquidator of the company.

- Besides, in the case of creditors' winding up, if the creditors so wish, a "committee of inspection" may be appointed to work along with the liquidators.

- **Notice to registrar:** A company of any resolution passed at the creditors meeting must be filed with the registrar within 10 days of the passing thereof. Otherwise fine of 500 Rs per day (s.501).

- **Appointment of liquidator (s.502):** The creditors and the members at their respective first meeting may nominate a person to be liquidator but should take the board of directors into considerations.

- **Committee of inspection (s.503)**: The creditors at their first or any subsequent meeting appoint a committee of inspection of not more than 5 members.

- **Fixing of liquidator's remuneration (s.505)**: The remuneration of the liquidator is fixed by the committee of inspection.

- **Board's power to cease on appointment of liquidator (s.505)**: All the powers of the directors should go to the liquidator.

- **Duty of liquidator to call meeting of company and creditors at the end of each year (s.508):** Within 3 months from the end of the year.

- **Final meeting and dissolution (s.509)**.

Voluntary winding up under supervision of the court:

- A voluntary winding up may be effected under supervision of the Court where an application to that effect is made by a creditor or a contributory or the company or the liquidator and the Court makes an order that the voluntary winding up should continue subject to the supervision of the Court.

- Such an order is passed by the Court where:

  a. the resolution for winding up was obtained by fraud, or
  b. the rules relating to the winding up order have not been observed, or
  c. the liquidator is prejudicial or is negligent in collecting the assets.

- The Court is also empowered under the section 527 to make an order for compulsory winding up superseding the order of winding up under its supervision.

Contributory:

- The term "contributory" is defined under section 428 to mean every person liable to contribute to the assets of a company in the event of its being wound up.

- The expression includes the holder of any shares which are fully paid up.

- A past member shall however be not liable to contribute if he ceased to be a member for one year or more before the commencement of the winding up.

2.9 CORPORATE GOVERNANCE

Meaning of corporate governance:

Corporate governance is the set of processes, customs, policies, laws, and institutions affecting the way a corporation (or company) is directed, administered or controlled.

Corporate governance also includes the relationships among the many stakeholders involved and the goals for which the corporation is governed. The principal stakeholders are the shareholders, the board of directors, executives, employees, customers, creditors, suppliers, and the community at large.

- A corporation is an organization created (incorporated) by a group of shareholders who have ownership of the corporation.
- The elected Board of directors appoint and oversee management of the corporation.

Definition:

- Defines "Governance" as the act, manner, fact or function of governing, sway, control.
- The word has Latin origins that suggest the notion of 'steering'. It deals with the processes and systems by which an organization or society operates.
- CG denotes direction and control of the affairs of a company and it is the relationship between the owners, directors and managers.

2.9.1 Main features of Corporate Governance

1. It is a set of system and processes which embraces organization structure.
2. Ensures best interest of the stakeholders.
3. Denotes direction leadership.
4. Explains relationship between directors, owners and managers.
5. Attempts to put a check on working of an organization.
6. Protects interests of bond holders and society.
7. To make balance between economic and social goals.
8. Ensures timely flow of all information to board of directors.
9. Ensures sound system of risk management and internal control.
10. Leads to transparency in working of corporate affairs.

Scope of CG:

It provides the structure for setting objectives and providing means to attain them.

2.9.2 Benefits of good CG

1. Reduces risk
2. Stimulates performance

3. Improves access to capital markets
4. Enhances the marketability of goods and services
5. Improves leadership
6. Demonstrates transparency and social accountability
7. Promotes transparency in decision making process

2.9.3 Steps for making Corporate Governance Efficient

1. Commitment of the management
2. Legal & administrative framework
3. Transparency in decision making
4. Proper implementation of codes
5. Improving the system
6. Reviewing banking system
7. Making laws effective
8. Strict compliance
9. Increasing role of independent directors
10. Highlighting governance role.

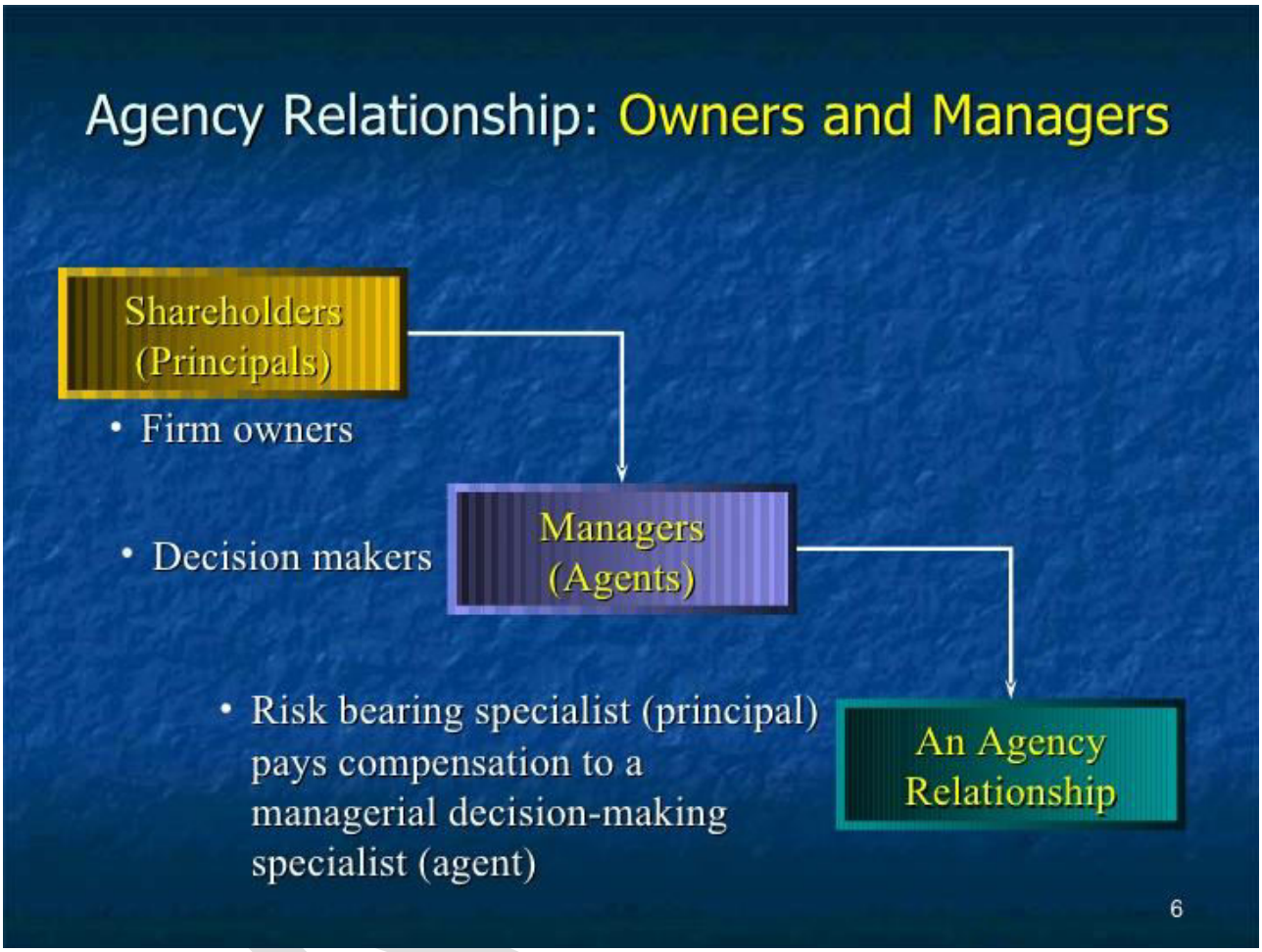
Activity Time:

"CORPORATE GOVERNANCE IS THE BLOOD THAT FILLS THE VEIN OF TRANSPARENT CORPORATE DISCLOSURE". EXPLAIN THE IMPORTANCE OF CG IN THIS CONTEXT.

2.9.4 Objectives of good corporate governance

- Strengthen management oversight functions and accountability.
- Balance skills, experience and independence on the board appropriate to the nature and extent of company operations.

- Establish a code to ensure integrity Safeguard the integrity of company reporting Risk management and internal control.
- Disclosure of all relevant and material matters Recognition and preservation of needs of shareholders.



2.9.5 Issues in corporate governance

- CG Is a system by which corporate entities are being controlled and directed. Corporate governance attempts to puts check on working of an organization .it checks the balance between directors, auditors and management. Corporate Governance is concerned with holding the balance between economic and social goals and between individual and public goals.
- The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources.

- The aim is to align as nearly as possible the interest of individuals, corporations and society.
- The foundation of any structure of corporate governance is disclosure.
- Openness is the basis of public confidence in the corporate system and funds will flow to centres of economic activity that inspire trust.
- Shareholders role in governance is to appoint the directors and the auditors.
- Poor corporate governance has ruined companies, sent directors to jail, and destroyed a global accounting firm and threatened economies and governments."

Parties to corporate governance:

- Board of directors Managers
- Workers
- Shareholders or owners
- Regulators
- Customers
- Suppliers
- Community (people affected by the actions of the organization)

2.9.6 Corporate social responsibility

- Proposes that a private firm has responsibilities to society that extend beyond making a profit.
- Obligation of firm decision makers to make decisions & act in ways that recognize the interrelatedness of business & society.
- It recognizes the existence of various stakeholders and firms deal with them.

Two Views of "who" are firms responsible to:

Traditional View:

- "There is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud" (M. Friedman, "The Social Responsibility of Business is to Increase Profits".
- By taking on the burden of social cost, the business becomes less efficient.
- Prices go up to pay for increased costs; or

- Investment in new activities & research is postponed.
- Firms are responsible to only their shareholders.
- Purely economic reasoning

Modern View:

- Business firms have four responsibilities:

  i. **Economic:** Produce goods & services of value to society so that the firm may repay its creditors and stockholders.

  ii. **Legal:** Defined by governments in laws that management is expected to obey.

  iii. **Ethical:** Follow generally held beliefs about how one should act in society

    - Work with employees & community in planning for layoffs, though no laws require this.
    - Many people expect firms to do these things.

  iv. **Open-mindedness:** Purely voluntary obligations a firm assumes.

    - Humanitarian contributions, training hard-core unemployed, providing day-care centres, etc.
    - Many people do not expect firms to do these things.

2.10 Amendment of Companies Act 2013:

The President of India accorded his assent to the Companies (Amendment) Act, 2017 (the "Amendment Act") on 3 January 2018. The Central Government notified the Amendment Act on the same day. However, the provisions of the Amendment Act will come into force on the date or the dates notified by the Central Government.

The impact of the changes on certain key aspects under the Companies Act, 2013 (the "Companies Act") are set out below:

1. Incorporation of a company and matters connected therewith.

The Amendment Act allows the promoters of a proposed company to reserve the name of the company for up to twenty days (from the earlier period of sixty days). The other procedural change in

relation to incorporation is that persons who are proposed to be appointed as the first directors are allowed to submit a declaration in lieu of an affidavit. Newly formed companies shall identify and communicate their registered office address within thirty days of incorporation to the Ministry of Corporate Affairs (the "MCA"), if not identified and communicated at the time of incorporation. It has now been clarified that the one hundred and eighty two days' period for determining the residency status of a resident director will apply proportionately in the case of a newly incorporated company.

2. Director Identification Number (DIN).

The Central Government may prescribe any identification number which shall be treated as the DIN for the purpose of the Companies Act. If an individual already holds or has acquired such an identification number, the requirement to obtain DIN, as it is currently understood, may stand discontinued. This is a welcome change given the elaborate procedure to obtain the DIN. One could expect the Central Government to approve the usage of Aadhaar number or PAN number as an alternative to the DIN in the days to come.

3. Key definitions.

a. The definition of the expression "significant influence" has been replaced with a new definition. Significant influence is to be now determined on the basis of control of at least twenty percent of total voting power or control of or participation in business decisions under an agreement. The erstwhile definition of the term "significant influence" had placed emphasis on total share capital as against the currently envisaged total voting power. This change would impact companies which have both equity shareholders and preference shareholders. The intent of the Amendment Act appears to be that significant influence is to be determined on the basis of voting rights exercisable by an equity shareholder only. However, this change would not impact preference shareholders when it comes to exercise of their voting rights in such matters where they are entitled to vote as per the law.

b. The expression "joint venture" has now been defined. It means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. The MCA had defined the expression "joint venture" in one of its earlier circular issued last year. The said circular was issued in the context of appointment of an independent director by unlisted public companies. Therefore, various stakeholders had voiced concerns about the application of this definition in contexts not dealt with under the said circular. This controversy has now been laid to rest.

c. An explanation has been inserted in relation to the definition of the expression "holding company". This clarifies the position with respect to an overseas parent company of an Indian company. Such companies would fall under the ambit of a "holding company" in terms of the Companies Act. Therefore, an overseas holding company will now be treated at par with an Indian holding company.

d. The definition of the expression "key-managerial personnel" now stands considerably enhanced. In addition to the existing category of persons, persons holding an office that is one

level below that of a whole-time director, and designated as a key-managerial personnel, by the board of directors of the company will also be considered as a key managerial personnel.

e. The definition of the expression "interested director" has been omitted. This addresses the drafting anomaly that was present in the original text of the law. In fact, the expression "interested director" has not been used in the Companies Act even once. Therefore, the definition was otiose. The concept of a director being interested is covered and dealt with under Section 184 of the Companies Act.

f. The ambit of the definition of the expression "related party" has been expanded as a new sub-clause (viii) has been inserted in Section 2 (76) of the Companies Act. The new sub-clause states that a body corporate which is a holding, subsidiary, fellow subsidiary or an associate company of an Indian company will also be treated as a related party of the Indian company and vice versa. In addition, a body corporate which is an "investing company or the venturer of the company" will also be treated as a related party of the Indian company. Investing company or the venturer of a company" means a body corporate whose investment in the company would result in the company becoming an associate company of the body corporate. However, in view of the earlier exemption granted to private limited companies, such persons will be not treated as a related party of a private limited company.

4. Meetings of shareholders.

An unlisted company can now hold its annual general meeting ("AGM") anywhere in India. Such companies are no longer required to hold their AGM at the registered office of the company or at some other place/address within the city, town or village where the registered office of the company is situated. The other procedural change with respect to an AGM is that the matter of ratification of the appointment of a statutory auditor need not be placed before the shareholders in each and every AGM. Companies that are one hundred percent held by an overseas body corporate can now hold their extraordinary general meetings overseas. Therefore, the rule that all companies need to hold their extraordinary general meeting in India has been relaxed.

5. Meetings of the board of directors.

The Companies Act had earlier prohibited the discussion of certain items in board meetings in which any director was participating through a video conferencing .

6. Facility.

In a significant departure, this restriction has been liberalized. If the quorum is being fulfilled by the directors who are physically present in a board meeting, the directors can deliberate on any matter, including the hitherto restricted matters.

7. Issue of securities.

The Amendment Act now provides that proceeds from a private placement of securities cannot be utilized till the return of allotment is filed with the MCA. Therefore, companies who were looking to

utilize share application money as a source of meeting their short term capital needs are no longer allowed to do so. In addition, the Amendment Act clarifies that an offer of shares cannot be renounced by the person to whom the offer is made. There was some ambiguity about this point in the context of a private placement of securities and this ambiguity has now been addressed. It has also been provided that a company can issue shares at a discount to its creditors when its debt is converted into equity pursuant to any statutory resolution plan or debt restructuring scheme in accordance with the Reserve Bank guidelines, etc. It is worth remembering that companies were otherwise not allowed to offer shares at a discounted price. This is a pragmatic change and offers the necessary flexibility in undertaking restructuring activities, particularly, in designing insolvency resolution plans. The earlier restriction that companies cannot issue sweat equity shares until the completion of one year from the commencement of business has been removed. This is a useful change, and is expected to benefit start-ups.

8. Loans to directors and to persons in whom the directors are interested.

In terms of the Amendment Act, a company is allowed to provide a loan (or issue a guarantee or security in connection with such a loan) to a person in whom any of the directors of the company are interested. However, in order to do so, two conditions are required to be fulfilled. The first condition is that the shareholders of the lender company shall have accorded their consent to the transaction through a special resolution. The second condition is that the borrower company should utilize the loan proceeds only for the purpose of its principal business activity (the expression "principal business activity" continues to remain undefined). This is an important and pragmatic change and will facilitate legitimate business transactions. The second condition as above would not apply in respect of transactions involving a holding company and its wholly owned subsidiary. The Amendment Act continues to prohibit the providing of loans to a director of a company or that of its holding company.

9. Clarification on disqualification of directors and the consequent vacation of their office.

In terms of Section 164(2) of the Companies Act, a person who is or has been a director of a company which has (a) not filed its financial statements or annual returns for any continuous period of three financial years or (b) has failed to repay the deposits accepted by it or pay interest thereon or to redeem any debentures on the due date or pay interest due thereon or pay any dividend declared and such failure continues for one year or more, is not eligible to be re-appointed as a director of that company or as a director of any other company. Section 167(1) states that if a director has incurred any of the disqualifications under Section 164, he / she shall automatically vacate office. The MCA was of the opinion that in view of the language of this section, a director would automatically vacate his / her office in all the companies in which such person was a director. This was creating a peculiar situation where the company in default under Section 164(2) was left without any director. Consequently, any new appointment would also be hit by the disqualification under Section 164(2). Therefore, an attempt has been made to clarify that the directors of such companies will vacate their office in all the companies except in the company which has committed the default under Section 164(2). Furthermore, persons who are appointed as a director of such a company will not incur the disqualification under Section 164(2) for a period of six months from the date of their appointment. The result of this is that persons agreeing to become directors a company which has committed a default under Section 164(2) should be very careful and diligent to regularize the non-compliances

within six months failing which the disqualification under Section 164(2) and the consequence under Section 167(1) will get attracted in their case.

10. Managerial remuneration.

The restrictions on payment of managerial remuneration have been rationalized. The approval of the Central Government is no longer required in respect of payment of managerial remuneration in excess of the limits prescribed under the Companies Act (that is 11% of the net profits). The matter of payment of managerial remuneration in excess of the limits is now allowed to be settled / decided at the shareholder level. If shareholders accord their approval, such proposals can be implemented without the approval of the Central Government. However, a company that has defaulted on its payment obligations to a bank / financial institution, secured creditor or the holder of non-convertible debenture can implement such a proposal only after obtaining the consent of such persons. The Amendment Act also clarifies that the applications pending with the Central Government as on date shall abate.

11. Consolidation of accounts.

Earlier, companies were required to consolidate the accounts of theirsubsidiary company along with theirs and lay the same before the shareholders in an AGM. This requirement has now been extended to include associate companies also. Therefore, companies will now be required to consolidate the accounts of both their subsidiary and associate companies in the same form and manner in which their financial statements are prepared. This requirement will create an additional compliance and reporting burden on the companies, especially given the broad ambit of what would constitute an associate company.

12. Foreign Companies.

The reporting and compliance burden on foreign companies stands enhanced. The provisions that were hitherto applicable only to foreign companies with a substantial Indian ownership has now been made applicable to all foreign companies (regardless of its ownership composition).

13. Compounding of offences.

The impact of the changes is that contraventions that were punishable with (i) imprisonment or fine; or with (ii) imprisonment or fine or with both, can now be compounded. The earlier position was that unless a contravention was punishable with fine only, such contraventions could not be compounded.

14. Forward contracts and insider trading.

Sections 194 (Prohibition on forward dealing in securities of company by director or key managerial personnel) and 195 (Prohibition on insider trading of securities) stand repealed. These sections were causing a lot of practical challenges in the context of private limited companies. Since listed companies are anyway subject to a securities law regime which deals with these aspects, these sections were not necessary in the first place.

Conclusion

The Amendment Act is an incremental and natural step towards liberalizing and rationalizing some of the aspects of the Companies Act. It also removes some drafting ambiguities plaguing the Companies Act. It has also sought to align the provisions of the Companies Act with other statutes, like securities laws and the regulations of the Reserve Bank of India. To that extent, it is a welcome step.

2.11 REFERENCE

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