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October 19, 2020

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The (Indian) Companies (Amendment) Act, 2020

Background:

The (Indian) Companies Act, 2013 (**the Act**), the primary legislation regulating companies operating in India, was substantially enforced with effect from April 01, 2014. Since then, it has undergone three rounds of amendments in 2015, 2017, and 2019, with the 2017 amendments being the most comprehensive. The Act has now been amended for the fourth time, by the (Indian) Companies (Amendment) Act, 2020 (**Amendment Act**). The Amendment Act was passed by the Parliament, pursuant to which it received the presidential assent on September 28, 2020. The provisions will be brought into force separately by way of notification. The Amendment Act is a culmination of the report submitted by the Company Law Committee (**CLC**) in November 2019.

The primary purpose of the Amendment Act seems to align the Act in line with the Indian Government's stated goal of promoting "*Ease of Doing Business*" in India. The CLC, set up by the Ministry of Corporate Affairs (**MCA**), Government of India, had submitted its report to the MCA in November 2019, recommending decriminalisation of 46 compoundable offences under the Act. This list was in addition to the 16 compoundable offences already decriminalised by the Companies (Amendment) Act, 2019.

In line with this recommendation, the Amendment Act has decriminalised 49 offences, which are compoundable under the Act.

The Amendment Act also addresses a long pending demand from the community of Independent Directors, that given the nature of responsibilities cast on them under the Act, and the liabilities that they incur, they deserve better remuneration. Pursuant to the amendment, Independent Directors will have a fixed remuneration, irrespective of profitability of the company, subject to the limits laid down under Schedule V of the Act.

The Amendment Act also permits Indian companies (whether listed or unlisted) to list overseas on foreign stock exchanges, which shall be permitted under the rules to be notified by the Government of India.
The Amendment Act also introduces a new chapter namely, XXIA, dealing with producer companies. These provisions were a part of the Companies Act, 1956, but were not introduced in the Act as it was decided at the time that a separate special act would be enacted for producer companies. However, it seems that there was a rethinking on the same, hence, we now see provisions related to producer companies being reintroduced by the Amendment Act.

Below is an analysis of the key amendments under the Amendment Act and its likely implications.

The key amendments are as follows:

a. Decriminalisation of offences

One of the major amendments introduced by the Amendment Act is decriminalising certain offences under the Act. Those offences are decriminalised which can be determined objectively in case of defaults and which otherwise lack any element of fraud or do not involve larger public interest. The Amendment Act decriminalises offences under the Act by adopting the following measures:

i. *Removing criminal offences*: The Amendment Act has omitted few offences dealing with non-compliance, which can be heard by the National Company Law Tribunal (the quasi-judicial body in India that adjudicates issues relating to Indian companies), with regard to winding up of companies, correcting the registers of security holders; and redemption of debentures.

ii. *Removing the provision of imprisonment and converting the offence into a civil wrong*: The Amendment Act has removed the provision of imprisonment from few of the offences, along with change in the nature of the monetary levy i.e criminal fine to a civil penalty.

iii. *Reconsidering fine amounts*: The Amendment Act has also reduced the quantum of monetary penalty associated with few of the offences. The amount imposed as a penalty for non-compliance is enhanced or reduced depending on the nature of the offence.

To put things into perspective, attempt to decriminalise business laws is not new to India. This process began with liberalisation of the Indian economy in 1991. The first commercial law that was decriminalised was the Imports and Exports (Control) Act, 1947. It was replaced by the Foreign Trade (Development and Regulation) Act, 1992, which decriminalised most of the offences relating to imports and exports. The most fundamental step in this direction was the replacement of the draconian Foreign Exchange Regulation Act (FERA), 1973, by Foreign Exchange Management Act (FEMA), 1999, which decriminalised offences relating to foreign exchange regulations.

There is no denying the fact that India's criminal justice system is badly choked, and it typically takes several years to get a final outcome. So, in principle, any step taken by the MCA to de-clog the criminal justice system is a step in the right direction. Moreover, proving a criminal offence requires the standard of proof to be beyond reasonable doubt, a much higher threshold than the balance of preponderance of probabilities standard adopted for civil wrongs. Many critics have, therefore, questioned the efficiency of criminal law in dealing with corporate misconduct. The opponents of decriminalisation have argued that businesses may treat civil penalties as part of cost of running a business, which consequently may not prove to be much of a deterrence.

Hence, in the Indian context, it is advisable that the law strikes a healthy balance between civil and criminal corporate sanctions. Offences that involve misuse of substantial amount of public money must be dealt with under regular criminal justice system.

CLC had recommended decriminalising only 'compoundable offences' under Section 441 of the Act. The said section defines compoundable offences as those which are not punishable with imprisonment only or punishable with imprisonment and also with fine. Offences which are non-compoundable will be dealt with under the regular criminal system as per the provisions of Code of Criminal Procedure, 1973.

b. *Relaxation for debt listed company*

The definition of 'listed company' under Section 2(52) of the Act has been amended to exclude certain companies, based on listing of certain securities on recognised stock exchanges as may be provided in the rules. It is expected that those companies maybe carved out, which have issued debt securities and are listed on a stock exchange to reduce the compliance burden on them. Previously, the definition of listed company under the Act also included private companies whose debt securities were listed on recognised stock exchanges. This resulted in stringent regulations and compliance requirements to be followed even by such private companies. The amendment is a welcome step as it was dis-incentivising for private companies from seeking listing of their debt securities, even though this was in the interest of the company and the security holder.

c. *Overseas listing of Indian companies*

In 2018, SEBI had constituted an expert committee to consider allowing Indian companies to list their equity shares on foreign stock exchanges, among other matters. Our Firm was a member of the expert committee and the committee's report recommended permitting overseas listing, including certain amendments in

this regard, which have now been proposed as part of the Amendment Act. Prior to the amendment, Indian companies could only access foreign equity capital markets by issuing depository receipts i.e. Global Deposit Receipts (**GDRs**) and American Deposit Receipts (**ADRs**).

Section 23 of the Act has been amended by the Amendment Act to permit public companies to list their securities on overseas stock exchanges. The class of securities and jurisdictions where such listing is permitted are to be prescribed separately. The Amendment Act also allows the Central Government to exempt the application of certain provisions of the Act in order to facilitate companies undertaking an overseas listing. This is a welcome step towards opening a new avenue for capital raising by Indian companies. This facility may be availed of by many leading unlisted companies.

As highlighted by the Ministry of Finance in its press release in March 2020, the amendment is expected to increase the competitiveness of Indian companies in terms of access to capital, broader investor base and better valuations. In line with these objectives, the rules to be prescribed by the MCA should be simple and not impose an undue burden on issuers. Further, amendments to tax and foreign exchange laws are also critical to ensure companies can use this avenue as a viable option to access capital.

The rules to be notified by the MCA would clarify the type of securities that will be allowed for overseas listing and the permissible stock exchanges. Further, this would require appropriate changes in the FEMA regulations (FEM (Non-Debt Instrument) Rules, 2019, and suitable changes in the Income Tax Act, 1961, on the lines of what was done for ADRs and GDRs. Implementation of the proposal may require amendment in the Depositories Act, 1996, as the current provisions only recognise Central Depositories Services India Ltd. (CDSL) and National Securities Depository Ltd. (NSDL) as depositories. Post the implementation, foreign depositories will have to be permitted to facilitate the overseas listing process.

Since the registered office of the company will be in India, the *situs* of the shares to be listed overseas will continue to remain in India. Consequently, this may require payment of stamp duty on issue of shares under the amended Section 9A of the Indian Stamp Act, 1899, with effect from July 01, 2020. The Government needs to grant exemption from payment of stamp duty on such shares to make the instrument attractive for Indian corporates.

There could also be inconsistency between the accounting standards followed in India by such companies and the accounting standard of the country where the securities are listed. Those conflicts arising out of the inconsistency in the accounting standards also need to be resolved.

The definition of 'listed company' under Section 2(52) of the Act reads as under:

""listed company" means a company which has any of its securities listed on any recognised stock exchange.

Provided that such class of companies, which have listed or intend to list such class of securities, as may be prescribed in consultation with the Securities and Exchange Board, shall not be considered as listed companies."

The definition of 'recognised stock exchange' under Section 2(73) of the Act reads as under:

""recognised stock exchange" means a recognised stock exchange as defined in clause (f) of Section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956)"

As per Section 2(f) of the Securities Contracts (Regulation) Act, 1956, *"recognised stock exchange" means a stock exchange which is for the time being recognised by the Central Government under Section 4.*

Listing compliances: Such companies shall be subject to listing regulations of the country where the securities are listed and those requirements may not be consistent with India's listing regulation i.e. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. It is expected that the Government will not insist on mandatory listing of shares in India, within a certain period of overseas listing as otherwise there could be potential conflicts between listing requirements in India and those applicable in overseas jurisdiction.

It is expected that the Government of India will address all the above aspects to facilitate the process of overseas listing. Unless the consequential changes are made in other legislation, this provision will not become operational like the provision of cross-border acquisitions under Section 234 of the Act.

d. Reduction in time limit for rights issue

Rights issue is one of the commonly used modes of raising funds amongst corporates. Previously, Section 62 of the Act, specified that the rights offer should be kept open for a minimum 15 days and not exceeding 30 days from the date of offer, and if no response is received during that period, the offer shall be deemed to have been declined. The Amendment Act enables the Central Government to prescribe by rules lesser number of days, to expeditiously complete the rights offer. This is a positive change and would help the companies to raise capital by faster completion of the process of rights issue.

e. Significant Beneficial Owners ("SBO")

The provisions related to SBO were introduced in the Act by the 2017 amendment. An attempt was made to operationalise these provisions, but due to drafting lacuna in the rules framed under the section, MCA was forced to give multiple extension of time, despite completely revising the rules in 2018. Even today, there are interpretative challenges in many aspects of those rules. It is interesting that Section 90 of the Act was amended in 2019 even before the said section was operationalised, and stringent provisions for criminal prosecution were introduced. Now, the Amendment Act decriminalises the said section, and has also significantly reduced the penalty prescribed.

Interestingly, a new sub-section has been added to Section 89 of the Act, dealing with the declarations pertaining to beneficial interest in shares. This new sub-section authorises the Central Government by notification to exempt any class or classes or persons from complying with the requirements of the Section, if it is considered necessary to grant such an exemption in public interest, either unconditionally or subject to such conditions as may be notified. It appears that the Government may be able to use this power to exempt SBOs from filing their declarations under Section 90 of the Act, as the definition of "beneficial interest" is common for both the sections.

f. Periodic financial statements of unlisted companies

A new Section 129A of the Act has been introduced to empower the Central Government to prescribe by rules such class or classes of unlisted companies that would be required to prepare the financial results of the company on such periodical basis as may be prescribed. It is also provided that such financial results would have to be approved by the Board of Directors and complete audit or limited review of such results will have to be filed with the Registrar of Companies within 30 days of the completion of the relevant period.

This is a salutary amendment as we have a large number of unlisted companies that are currently required to publish their financial results only once a year. These companies are systemically important and have significant exposure to public funds. Public interest requires that such companies need to adhere to much stronger financial discipline in terms of publication of their results at more frequent intervals.

g. *Corporate Social Responsibility ("CSR")*

The Amendment Act has amended Section 135 of the Act dealing with CSR. It is now provided that if the company has spent excess amount in any financial year, beyond the 2% statutorily mandated CSR contribution, then such company can adjust the amount of CSR spend in the subsequent years to set-off the excess amount spent. This is a very positive amendment and it will encourage large companies to undertake major CSR projects like construction of hospitals, setting up of schools, etc., which requires large capital outlay.

Interestingly, while the quantum of penalty prescribed under different provisions of the Act has been significantly reduced, an exception is made for violation of Section 135 of the Act, whereby stringent penalty has been prescribed on the company as well as every officer of the company who has been in default. The Government is also proposing to amend the CSR rules and draft CSR rules have already been placed for public comments, which propose significant changes in the current regime. Hitherto, public charitable trusts were permitted to be implementing agencies for CSR expenditure to be incurred by the company, but now it is proposed to permit only company licences under Section 8 of the Act as non-profit organisation or an entity established by the Central or State Government and duly registered with MCA for carrying out CSR activities, to act as implementing agencies. This will have far reaching implications for those corporate houses, which are currently doing their CSR activities through public charitable trusts.

The Amendment Act also exempts the requirement of constituting a CSR Committee in case the amount to be spent by the company does not exceed more than INR 50 lakh. In such a scenario, the Board of Directors of the company can discharge such function of the CSR Committee.

h. *Remuneration of Non-Executive Directors and Independent Directors*

Prior to the amendment, the Act permitted only payment of sitting fees (capped at INR 1 Lakh per meeting) and commission on net profits of the company

not exceeding 1% or 3% of the net profits (as per Section 197 of the Act), depending on whether the company has a managing/ all-time director. Independent Directors were entitled to only sitting fees when the company had incurred loss or inadequate profit. Pursuant to the Amendment Act, a fixed remuneration will be given to Non-Executive Directors and Independent Directors, irrespective of profitability of the company, but subject to limits laid down under Schedule V of the Act. Section 197 of the Act has been amended to enable companies, to pay fixed remuneration to Non-Executive Directors, including Independent Directors, even in a situation where the company has not made any profit or has made inadequate profit.

i. *Benches of National Company Law Appellate Tribunal ("NCLAT")*

In addition to the duties under the Act, NCLAT also acts as an appellate body for appeals against orders passed by the NCLT under the Insolvency and Bankruptcy Code, 2016, and the appeals against the orders passed by the Competition Commission, under the Competition Act, 2002. Given the increasing workload of the NCLAT in New Delhi, the Amendment Act empowers the Central Government to establish additional benches of NCLAT. In fact, the Government of India has already issued a notification establishing an NCLAT in Chennai. This amendment will help to reduce the workload of the NCLAT's principal bench in New Delhi. Additionally, the ceiling on the maximum strength of the members of NCLAT under Section 410 of the Act has also been omitted by the Amendment Act.

j. *Punishment for wrongful withholding of the property of the Company*

Section 452 of the Act (which corresponds to Section 630 of the Companies Act, 1956) provides for punishment to any officer or employee of a company for wrongfully obtaining possession of any property, including cash, or wrongfully withholding the property. The Amendment Act now provides that the imprisonment of such officer or employee shall not be ordered if the court is satisfied that the company has not paid to that officer or employee his dues towards provident fund, pension fund, gratuity fund, or any other fund established for the welfare of officers or employees maintained by the company, or any compensation under the Workmen's Compensation Act, 1923, in respect of death or disablement. While the object seems to be laudable, there is a possibility of such provisions being misused by those ex-employees/ officers for holding onto company provided accommodations, even after retirement, resignation or termination by creating false disputes with regard to the amounts payable.

Impact on foreign companies

The Government of India's aim to promote foreign investment and to further ease of doing business has led to decriminalising and liberalising India's company law regime. Prior to the amendment, the Act comprised of various criminal penalties for minor and technical non-compliance. Owing to such penal provisions in the Act, the investors were deterred from investing. The decriminalisation of offences under the Amendment Act will help in reducing the prolonged criminal proceedings and clear the case backlog, which exists in the judicial system. Such backlog acts as a deterrence as the possibility of getting stuck in long-lasting litigation is high. Decriminalisation of offences under the Act is likely to yield intangible benefits in the form of protection of goodwill of a company that could otherwise get tarnished by criminal sanctions being imposed for minor, technical or inadvertent lapses, leading to reputational damage. As the CLC Report observed, while criminal sanctions are more grievous and permanent in nature, the cost of civil penalties maybe absorbed as part of running a business in the ordinary course. Moreover, the subsidiaries of foreign companies in India will also benefit from the changes proposed by the Amendment Act. Given the economic impact of COVID-19, the amendments brought in by the Amendment Act will help safeguarding investors against criminal liability for minor non-compliances. This will also result in increase of foreign investment, which will boost India's economy. Certainly, the changes proposed by the Amendment Act have the potential to confer long-term benefits on stakeholders and investors by facilitating ease of doing business and providing a swifter redressal and enforcement mechanism for corporate non-compliances in India.

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