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Company Law Committee Recommendation to amend the Companies Act, 2013

Ministry of Corporate Affairs, on 13th April 2022, has published 'Company Law Committee (CLC) Report 2022' for public comments. Vide this report, lot of recommendations are being proposed for amendment to Companies Act, 2013 (the Act). These recommendations can be broadly basketed into those relating to ease of doing business, restoration of some provisions of Companies Act, 1956, towards digitisation, strengthening corporate governance framework, etc.

This MMJC insight covers the key changes recommended in the CLC Report and divided into 3 parts viz.,

1. **New concepts recommended**
2. **The recommendations of CLCw.r.t. strengthening Corporate Governance**
3. **The recommendations of CLC w.r.t. Digitisation**

1. New concepts recommended

Particulars	Recommendations of company law committee (CLC)	Observations/remarks
Recognising issuance and holding of fractional shares.	• A fractional share means a portion of share less than 1 share unit. • Issue and holding of such shares are presently prohibited under the Act. • The CLC recommends that provisions relating to issue holding& transfer of fractional shares, in dematerialised form, should be inserted in Companies Act. • This recommendation only pertains to fresh issue of fractional shares by the company and not to cases where fractional shares get created on account of any corporate action.	The rationale behind introducing fractional shares is that the retail investors who are not able to invest in good shares due to their high price, can invest in the same. It will be interesting to know the regulatory aspects w.r.t. various shareholders rights, compliances arising from it and for which classes of companies it will be allowed.
Recognising issuance and holding of estricted	• RSUs &SARs are employee benefit plans like ESOP. • They are governed by SEBI (SBEB) regulations	Restricted Stock Units (RSUs) and Stock Appreciation Rights (SARs) are on similar lines of ESOP. There are some

Stock Units (RSUs) and Stock Appreciation Rights (SARs)	• There exists no provision in this regard in Companies Act as Sec. 62(1)(b) of the Actdeals only with ESOPs. • CLC proposes that RSUs & SARs should be recognised under Companies Act and accordingly enabling provisions to issue and procedure to issue should be laid down and their issuance be sufficiently encumbered.	technical differences related to taxation etc. but the basic concept is that they give the employees a right to hold shares of company subject to certain conditions. The Act permits to issue ESOPs to only permanent employees only. Whereas SARs and RSUs can be given to all employees.
Easing the requirement of raising capital in distressed companies (issuing shares at a discount)	• Section 53 of the Act prohibits the issue of shares at discount that is below nominal value or face value. • CLC recommends that the distressed company be allowed to issue shares at discount to specified persons on the condition that such issues be valued by registered valuers failing which the issue shall be void.	• This provision is not totally new as it existed in Sec. 79 of Companies Act 1956 where issue at discount was allowed after obtaining approval from Company Law Board (CLB). • Distressed Company may be categorised as such classes of companies that have cash losses (other than depreciation and revaluation reserves) for previous 3 consecutive F.Y or more and fulfil such terms and conditions and issue shares in such manner as may be prescribed by Central Govt. • It will be interesting to know whether the Companies which are in the CIRP (IBC) process can also be able to issue shares at discount.
Recognising Special Purpose Acquisition Companies (SPAC)	• Special Purpose Acquisition Company (SPAC) is a company who does not have an operating business and is formed for acquiring a target company. • CLC recommends inclusion of provisions recognising SPACs under Companies Act and allow entrepreneurs to list Indian incorporated SPAC on	SPAC provides its target company, advantage of listed company without going through formalities and rigours of IPO. Regulations governing SPAC already exist in International Financial Service Centres Regulations. Further, the market regulator SEBI is deliberating on bringing regulations for governing working of SPAC in

	domestic and foreign exchanges. • It also recommends that, requirements of conducting business before striking-off SPAC should be relaxed & provision for giving an exit option to dissenting shareholders of SPAC if they disagree to the choice of target company identified, should be included in Companies Act.	India. There is a need to notify the commencement of amended Sections 23(4) and Section 23(5) of the Actwhich deals with listing of Indian companies in Foreign jurisdiction
Allowing companies to re-align their financial year	• Any company who is a holding/subsidiary/associate of a foreign entity, may follow a different financial year in order to consolidate its accounts with such foreign entity by taking approval of NCLT. • In case if the Indian company ceases to be associated with such foreign entity, then there was nowhere clearly mentioned about how to revert to normal financial year (1st April to 31st march). • Therefore, the CLC has recommended to provide a procedure to revert the financial year in such cases by making application to Central Govt.	This is a step taken towards ease of doing business as many such companies face ambiguity as to which financial year should they follow after getting disassociated with foreign entities.
New concept of Producer LLPs	To enable producer institutions to take advantage of the light touch regime under LLP Act, 2008, the CLC has recommended that Producer LLPs should be allowed to be incorporated under such Act. CLC has also recommended that this should be supported by a model LLP Agreement for guiding the decisions of the Producer LLP and ensuring smooth functioning.	A new chapter is proposed to be inserted in LLP Act, 2008, it is interesting to know how the mutual assistance principle and voluntary membership which is a feature of producer organization will be taken care of while introducing provisions w.r.t it in LLP.

2. The recommendations of CLC w.r.t. strengthening Corporate Governance

Particulars	Recommendations of company law committee (CLC)	Observations/remarks
Strengthening audit framework – Prohibitory list – Non-Auditservices	• Amendment to Sec. 144 of the Act -Enabling provision to prescribe a differential list of prohibitions on availing non-audit services for certain classes of Companies	Rationale is to restrict certain companies involving public interest from availing any non-audit services of any kind, directly or indirectly and permitting certain companies that do not have a public interest to avail certain non-audit services also from auditor.
Strengthening audit framework – Resignation by auditors	• The resigning Auditor should assure the shareholders and other stakeholders that, in her opinion, there is nothing in the company's accounts which needs to be brought to their notice, and that her resignation is an independent decision. The auditor shall be under an explicit obligation to make detailed disclosures before resignation. • Specific mentioning to be done about whether such resignation is due to non-cooperation from the auditee company, fraud or severe non-compliance, or diversion of funds. • Moreover, if such information comes to light after the resignation of an auditor but has not been disclosed in the resignation statement, suitable action may be taken against theresigning auditor.	However, it is yet not clear that which authorities will take action in case of failure to give such disclosure by resigning auditor.
Strengthening audit framework – Joint Audit	• Enable CG to prescribe mandatory joint audit for certain classes of companies and the provisions concerning the liability of individual	The deliberation about joint audit was being carried out by ICAI but there were implementation issues. Currently Insurance Companies, PSU Banks and

	auditors should also be accordingly provided in CA-13	entities having asset size of 15000 crore or more are required Joint Audit mandatorily as per RBI guidelines.
Strengthening audit framework – Auditor of holding company to comment on true and fair view of each subsidiary company	• Since a holding company makes significant investment in its subsidiary companies, there should be proper oversight, especially on financial matters, of such subsidiary companies by the Board and the auditor of the holding company. • Suitable amendments may be required to ensure that the auditor of the holding company has been given assurance about the fairness of audit of each subsidiary company by the respective auditors. • In addition, the auditor of the holding company may also be empowered to independently verify the accounts or part of accounts of any subsidiary company.	In the case of holding companies while the auditor of the holding company has been given the right of access to the records of subsidiary companies, there is currently no statutory obligation or liability on the auditor of the holding company (principal auditor) to formally verify and confirm on the truthfulness and fairness of accounts of subsidiary companies. Hence this provision is recommended.
Strengthening audit framework – Forensic Audit	• Forensic audit may be ordered during investigations, of such nature as may be prescribed, under Chapter XIV of CA-13. The Central Government should have the power to prescribe detailed Rules for thispurpose through subordinate legislation.	Presently such audit is being conducted on the specific directions of regulators or on demand of creditors. A view was made that there should be clarity on the trigger event for ordering forensic audit and there should be uniformity on this across all regulators.
Cooling-off period before auditors become directors	• To uphold the independence of auditors, the Committee recommended the insertion of a mandatory one-year cooling-off period, from the date of cessation of office, only after which an auditor of a company may be	An appropriate disqualification is also proposed to be inserted in Section 164(1)(a) of the Act in this regard. The amendment shall also provide that such a restriction will only apply to the auditing partner in the case of an

	permitted to hold the position of a NED, MD, WTD in the same company or its holding company, subsidiary company(ies), fellow subsidiary(ies) or associate company(ies).	audit firm structured as a partnership/LLP
Standardising qualifications by auditors	• To ensure greater clarity, disclosure and standardisation, the Committee proposed that an enabling provision be inserted in CA-13 to allow the Central Government to introduce a format for auditors to provide the impact of every qualification or adverse remark on the financial statements of the company for circulation to the Board before the same is passed on to shareholders.	Auditors' reports often highlight reservations or adverse remarks regarding a company's financial statements. It was apprehended that such remarks do not sufficiently elaborate on the corresponding negative effect on the economic health or functioning of the company.
Setting up of Risk Management Committees (RMC)	• To strengthen the Board's power to overview and supervise risk management systems, the Committee recommended the inclusion of new provisions in CA-13 for the constitution of an RMC for such class or classes of companies, as may be prescribed by the Central Government	This is in line with SEBI (LODR) Regulations, 2015 which requires top 1000 listed entities to set up an RMC of directors
Cooling off period before an ID becomes a Managerial Personnel	• Mandatory one year cooling off period from the date of cessation of office, after which an ID nay be permitted to hold the position of an MD, WTD or Manager in the same Company or group of companies	Earlier there was a cooling off period in case of appointment of ID after completion of tenure, but a cooling off period in this regard was not provided. This is in line with an amendment in SEBI LODR Regulations by inserting a similar provision in Regulation 25(11) with effect from 1 January 2022.
Clarifying on Tenure of ID	• Clarification that the period during which the ID functioned as an additional director before approval of	In some companies, there might be a practice of the Board of directors appointing a person as an additional

	shareholders for his / her appointment shall be included while computing the total tenure of the ID of maximum 5 years.	director in the capacity of ID, subject to approval by shareholders in the next meeting; and thereafter the shareholders might approve the appointment of ID for a period of 5 years from the date of annual general meeting (AGM) till the AGM to be held in the sixth year considering the AGM where he is appointed as first year. In such cases, now it is clarified that the tenure as an additional director will also becalculated in tenure as ID.
Disqualification and Vacation of office of Director	• If the defaults under Section 164(2)(b) of the Act are not satisfactorily remedied, the newly appointed directors would be liable for automatic disqualification upon the completion of two years instead of six months from the date of appointment.	Earlier six months period was provided to newly appointed director in case of defaulting company u/s 164(2)(b) of the Actwhich might not have been sufficient, especially in cases where the disqualification might have arisen due to non-repayment of deposits/ debentures / dividend. Therefore,it is recommended to extend period from 6 months to 2 years and upon completion of 2 years, if the default is not made good, then he will be automatically disqualified.

3. The recommendations of CLC w.r.t. Digitisation

Particulars	**Recommendations of company law committee (CLC)**	**Observations/remarks**
Communication in electronic form (Sec. 20)	Sec. 20 of the Act stipulates different modes by which Document can be served Further Sub-sec (2) of Sec. 20 of the Act allows member to request the delivery of any document through particular mode by bearing the fees which company may determine in its AGM	This is a step towards ease of doing business and it will reduce the burden of cost on Company. Postal delivery of documentsshould remain available wheremembers have specificallyrequested to receive suchdocuments also in physical form.

	Presently there is a provision in Section 20 for providing certain documents in electronic mode. But it is voluntary. A specific provision is recommended for enabling the Central Government to prescribe Rules for such class or classes of companies for to serve such documents as may be prescribed to all their members in **electronic mode only** for compliance with the provisions of the Act. Further it is also recommended that the fees which can be charged for delivering the documents may be determined in any general meeting. Presently as per proviso to Section 20(2) of the Act, the fees could be determined only in annual general meeting.	
Holding general meetings through the use of technology	The CLC has recommended that suitable provisions of Companies Act to be amended to allow conduct of general meetings (EGMs as well as AGMs) physically, virtually,and in hybrid mode. It is also recommended that in case of EGM to be conducted entirely through electronic mode, the notice period for such meetings should be shortenedtosuch period as may be prescribedby the Central Government. The Central Government is expected to make suitable provisions through Rules in this behalf.	During the out-break of Covid-19 pandemic, MCA had permitted conduct of general meeting through video conferencing (VC) or other audio-visual means (OAVM). This amendment is proposed on same grounds.

Maintaining statutory registers through an electronic platform	The CLC has recommended that some specified classes of companies should mandatorily maintain their statutory registers on an electronic platform in the manner laid down by central government.Forthis purpose, the CentralGovernment may set up anelectronic facility. No one including the central government in ordinary course, should be allowed to access the information without company's authorisation. However, in the case ofcertain enforcement-related functions, Central Government may be allowed to direct the company to share the information held on the statutory registers.	The company should be able to share the information therein with members and others as and when required by masking the information which is not needed to be shared. However, the government is required to look after adequate security of information.
Facilitating e-enforcement and e-adjudication	CLC recommended to amend Section 398 of the Act so as the Explanation under Section 398which is roadblock towards implementation of e-enforcement be omitted and to give an enabling power to government to make Rules for electronically imposing fines, penalties and payment of fees	It is to enable the Central Government to make rules for conducting enforcement related actions in transparent and non-discretionary manner with a proper trail through an electronic platform

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Contributors:

Deepti Jambigi Joshi
Partner
deeptijambigi@mmjc.in

Vrushali Bhave
R&D Team
vrushalibhave@mmjc.in