



Companies Act 2013:
Provisions affecting Private Limited Companies

Mulund CA CPE Study Circle of WIRC of ICAI
 Saturday, July 5th, 2014

Nilesh S Vikamsey Companies Act, 2013 1

Agenda for Today's Meeting

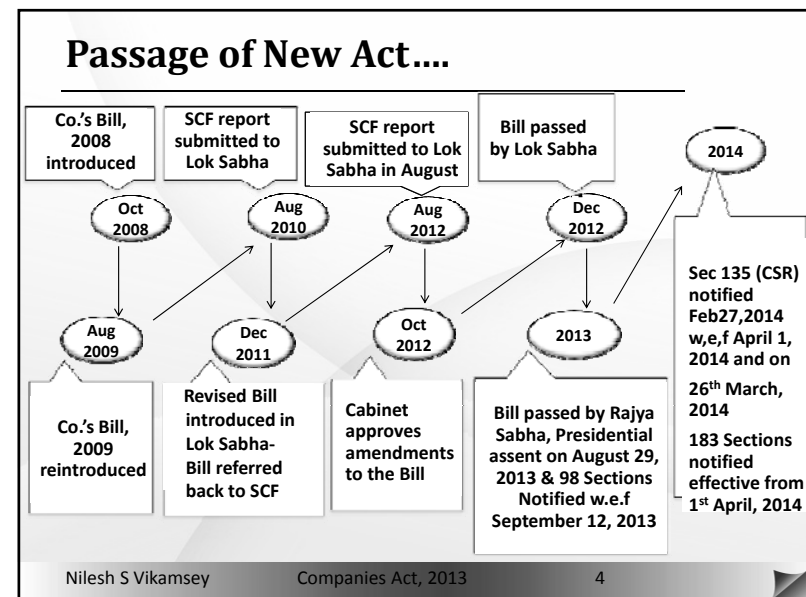
- 1 Introduction and Structure
- Impact on Private Companies
- Funding by Holding Company
- Related Party Transactions
- Loan to Directors
- Restrictions on inter-corporate loans & advances
- Acceptance of Deposits
- Subsidiary & Associates

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Agenda for Today's Meeting Cont'd..

- 1 Accounts of the Company
- Depreciation
- Bonus Shares
- Revision & Reopening of Accounts
- Audit & Auditors
- One Person Company , Small Company & Dormant Company
- Private company Vs. LLP

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Structure

**The Companies
Act, 1956**

**18 Chapters
658 Sections
15 Schedules
67 Definitions**

**The Companies
Act, 2013**

**29 Chapters
470 Sections
7 Schedules
95 Definitions**

Almost 75% of the Sections contain the words “to be specified” or “as may be prescribed”– depicting extensive “delegated legislation”. The final Rules are now available on almost all provisions which are effective from April 1, 2014

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5

Structure...continued

Substantial Portion of the Act by way of rules

Imprisonment around 75 times referred to in the Sections

Special resolution – around 42 times referred to in the Sections

Prosecution – around 24 times referred to in the Sections

CG Approval around 8 times referred to in the Sections

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6

Structure...continuedfor Highlights

Mandatory CSR

Enhanced Accountability on Corporates

Independent Director – Detailed provisions & code for ID

NFRA (replacing NACAS) given more powers

Additional disclosures in BoD Report

Restriction on Inter Corporate Loans/Investments and Guarantee

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7

Structure...continuedfor Highlights

M & A procedures streamlined

1 Woman Director mandatory in prescribed class of Companies

Mechanism for Class action suits provided in the Act

NCLT given very wide powers

Transfer of shares to IEP Fund along with unpaid/unclaimed dividend

Changes in Depreciation Provisions

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8

Structure...continuedajor Highlights

Private placement clearly defined

Several exemptions /relaxations / privileges to Pvt Co now withdrawn & permissible max no of members increased from 50 to 200

Concept of One Person Company (OPC) introduced

Small Companies defined and granted some relaxations

Many new definitions and changes to existing definitions inserted



IMPACT ON PRIVATE LIMITED COMPANIES

Exemptions etc... Withdrawn

➤ Further issue of Share Capital by Right issue

Sec. 81 { • Applicable only to Public Co.'s

Sec. 62 { • Now Applicable to Private Co.'s also

Additional changes:

- if not right issue then:
 - to any person if authorized by Special Resolution;
 - at a **price to be determined by registered valuer &**
 - subject to other conditions as may be prescribed [Rule 13 of Companies (Share Capital & Debentures), Rules, 2014

Exemptions etc... Withdrawn

- In case the existing shareholders do not accept the offer, directors should dispose such shares in a manner “**non disadvantageous**” to the **shareholders and company**. Earlier it was to be disposed of in manner “**most beneficial to the company**”
- Under the existing provisions Sec. 81 (1A) (b)-if the approval was given by simple majority, CG could have allowed the issue if it was shown to be most beneficial to the Company. Such option of CG approval is removed in the New Act
- Draft notification u/s 462 dated June 24, 2014-
62(1)(b)- deals with ESOP. Following modification:- Shall apply except that instead of special resolution, ordinary resolution would be required

Exemptions etc... Withdrawn.... Cont'd

➤ Restrictions on Kinds of Capital that can be issued

- Sec. 86 { • Applicable only to Public Co.'s
- Sec. 43 { • Now Applicable to Private Co.'s also

➤ Length of Notice of GM, explanatory statement, Quorum, Chairman, Proxies, Voting, poll

- Sec. 171-186 { • Applicable only to Public Co.'s
- Sec. 101-109 { • Now Applicable to Private Co.'s also

Draft notification u/s 462 dated June 24, 2014- S. 43 Kinds of S/C & S.47 Voting right shall not apply fully

S. 101 to 107 & 109- Shall not apply unless otherwise specified in respective sections or unless articles of the pvt Co. otherwise provide

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Exemptions etc... Withdrawn.... Cont'd

➤ Interested director not to participate or vote in Board's proceedings

- Sec. 300(2) { • Applicable only to Public Co.'s
- Sec. 184 { • Now Applicable to Private Co.'s also

➤ Appointment & tenure of Managing Director

- Sec. 269 (2) & 317 { • Applicable only to Public Co.'s
- Sec. 196 & 203 { • Now Applicable to Private Co.'s also

Draft notification u/s 462 dated June 24, 2014- Appointment of MD and WTD 196(4)(5)- Limits on managerial remuneration as per S. 107 are not applicable to Pvt Co as S. 197 refers to Public Co only but in S. 196(4) there is ref of S.197. Hence it is now clarified that (4)&(5) shall not apply to Pvt Co

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14

Exemptions etc... Withdrawn.... Cont'd

▪ Other conditions:

- Age limit of 21 to 70
- If age > 70 approval by S.R in G.M no further approval of the C.G shall be necessary for such appointment
- MD and Manager both cannot be appointed in same company
- Term of MD for 5 years

➤ Appointment of Director

- Sec. 264 { • Applicable only to Public Co.'s
- Sec. 152 { • Now Applicable to Private Co.'s also

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Exemptions etc... Withdrawn.... Cont'd

➤ Deposit from members

- Sec. 58A { • Deposits from members by Pvt Co. was exempt
- Sec. 73 & 74 { • Stringent conditions prescribed for deposit from members (discussed in details in forthcoming slides)

➤ Consent to act as director to be filed with the ROC

- Sec. 264(3) { • Applicable only to Public Co.'s
- Sec. 152 { • Now Applicable to Private Co.'s also

Draft notification u/s 462 dated June 24, 2014- S.73(2)-Shall not apply to pvt co.'s having 50 or less no. of mem. if they accept monies from their members not exceeding 25% of aggregate of paid up capital & FR or 100% of the paid up capital, whichever is more, & which inform the details of such monies to the RoC in the prescribed manner

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16

Exemptions etc... Withdrawn

➤ Commencement of business

- | | | |
|----------|---|--|
| Sec. 149 | { | • Applicable only to Public Co.'s |
| Sec. 11 | | • Now Applicable to Private Co.'s also |

Sec 11(1)- Co. having a S/C not to commence any business or exercise any borrowing powers unless-

- Declaration filed with the ROC that every subscriber to the MOA has paid the value of the shares agreed to be taken by him
- Co. has filed with ROC verification of its Registered office

Sec 11(3)- If declaration is not filed within 180 days of incorporation and ROC has reasonable cause to believe that the co. is not carrying on any business or operations, he may, initiate action for the removal of the name of the company from the Register of Co.'s.

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17

Exemptions etc... Withdrawn

➤ Passing of Resolution by Postal Ballot

- | | | |
|-----------|---|--|
| Sec. 192A | { | • Applicable only to Public Co.'s |
| Sec. 110 | | • Now Applicable to Private Co.'s also having > 50 members |

Following items of business shall be transacted only by means of voting through a postal ballot-

- Object Clause Alteration
- Articles of Association Alteration
- Change in Registered Office outside local city limits
- Change in utilisation of funds raised by company from public
- Issue of shares with differential voting rights
- Variation in the rights attached to shares or debentures or other security
- Buy back of shares

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Exemptions etc... Withdrawn

- Election of small shareholder's director
- Sale of undertaking
- Giving loans or providing guarantee or security in excess of limits under Section 186

NOTE : Not applicable to OPC or companies having upto 200 members

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19

Restriction on Non-cash transaction involving directors (S. 192)

The new Act introduces the new requirement, that without prior approval of the company in general meeting, a company will not enter into an arrangement by which:

- A Director of the company or its holding, subsidiary or associate company or a person connected with him acquires or is to acquire assets for consideration other than cash, from the company; or
- The company acquires or is to acquire assets for consideration other than cash, from such director or person so connected

If the director or connected person is a director of its holding company, approval under this sub-section shall also be required to be obtained by passing a resolution in general meeting of the holding company

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20

Private Placement (Section 42)

- Offer / invitation in a financial year not exceeding **200** persons (separately for each kind of security) or as may be prescribed (excluding QIB, employee under ESOP), **else it is offer to public**
- **Payment** through cheque or DD or other banking channels but **not by cash**
- Allotment in 60 days from the receipt-else repay the money in 15 days. Interest @ 12% p.a. to be paid if refund is belated
- Application Moneys to be kept in a separate bank a/c in scheduled bank, not to be used for purpose other than allotment or repayment
- Offer in person by name and records thereof and Application Form-PAS-4 to be serially numbered
- No advertisement or the use of any media/ marketing or distribution channels or agency
- Investment size – not less than Rs. 20,000 of face value

Consequences of non compliance:

- Penalty - higher of amount involved in offer or Rs 2 crores
- Refund of all the money in 30 days

The ongoing case of Sahara India pertained to breach of 'Private Placement' under the Old Act

Other Major Provisions

1956 Act, Sections	2013 Act, Sections	Particulars
300 (1)	2 (49)	Interested Directors
2 (29A)	2(57)	Definition of Net Worth- No change "the aggregate value of the paid-up S/C and all reserves created out of the profits and S.P account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation"
2(31)	2(60)	Officer in default
26-29	5	Entrenchment provisions can be put in AA
-	186	Loans etc by holding Co. to WO's

BOARDS AND DIRECTORS



Major new definitions

Promoter [Section 2(69)] - the definition of promoter has been introduced to also include a person—**(Notified on 12th September, 2013)**

- (a) who has been named as such in a prospectus is identified by the company in the annual return
- (b) who has **control over the affairs of the company, directly or indirectly** whether as a shareholder, director **or otherwise**; or
- (c) in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act:

Provided that nothing in sub-section (c) shall apply to a person who is acting in a professional capacity;

Board of Directors

1956 Act	2013 Act
Maximum no. of directors in a Co can be 12 [Section 259]	Now increased to 15 , with SR at GM -no. can be > 15 [Section 149]
Max number of directorship a person can have is 15 (excluding private co etc.) [S. 276]	Restricted to 20 (with max 10 public co.'s) [Section 165]. Time of 1 year given to comply
Director of the company to be resident in India - No specific provision	1 of directors - stayed in India for 182 days or more in previous calendar year (S.149)
Formation of AC must for Co having paid up capital > Rs 5cr (S.292A)- no specific provisions for Nomination & Remuneration Committee OR Stakeholders Relationship Committee	All listed Co & other Public Co having, at least Rs.10Cr or more paid up share capital, turnover of Rs.100 Crores or more, loans or borrowing or debentures or deposits of Rs.50 Crores or more are required to have AC and Nomination & Remuneration Committee. Stakeholders Relationship Committee for a company having > 1000 Shareholders, Debenture holders, deposit holder & other such securities [Sec 177 & 178] & Vigil Mechanism for listed Cos & Cos accepting deposits or borrowing from Bank or FI's > 50 Crores
No such Provision	Resignation of director S.168- Concerned Director to file form with RoC along with detailed reason (notified)

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25

Powers of BoD

1956 act (Sec 293)	2013 act (Sec 180) (Notified on 12th September, 2013)
Section 316 & 317 rws Sec 269- Appointment of MD or WTD- in case of Public Co.'s	Sec 203- All listed co.'s & other Public co.'s having paid up S/C> 10crore to have 1 MD or WTD and CS and CFO
Restriction on powers of the Board applied only to Public Companies	Applicable to all Companies. Exemption to Private Co.'s taken away (S. 179)
Required ordinary resolution to exercise certain powers	Required special resolution to exercise certain powers—Sell, lease, Disposal of Undertaking. Investments & borrowings more than net worth, investment of compensation received in M&A (Slightly different words from 293) ,remit or give time for repayment of directors due.

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26

Powers of BoD

1956 act (Sec 293)	2013 act (Sec 180)
expression "undertaking" and substantially the whole of the "undertaking" used- not defined	180(1) undertaking means an undertaking in which the investment of the Co. > 20% of its net worth as per the audited balance sheet of the preceding F/Y or an undertaking which generates 20% of the total income of the company during the previous F/Y Substantially the whole of the undertaking in any financial year shall mean 20% or more of the value of the undertaking as per the audited balance sheet of the preceding F/Y
Contribution to any Charitable Fund > 5% of avg net profit for last three years – General Meeting Resolution required	S. 181 (contribution to Charitable Funds) & S. 182 (contribution to political parties) are applicable to all Companies

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27

Report of Board of Directors

Additional Items required to be given in report of board of Directors:

- The extract of the annual return
- Particulars of loans, guarantees or investments in subsidiaries as provided in sec. 186
- Particulars of contracts or arrangements with related parties with rationale for arms length pricing as stated in sec. 188
- A statement indicating development and implementation of risk management policy for the company which in the opinion of the Board may threaten the existence of the company
- The details in respect of adequacy of internal financial controls **with reference to the financial statements**
- CSR if not spent or less spent – reasons & rationale to be disclosed
- Other items specified in Rule 8 of Companies (Accounts) Rules, 2014

Additional Items required to be given in director responsibility statement:

- Details about policy developed and implementation of CSR policy
- Directors had devised proper system to ensure compliance with the provision of all applicable laws and that such systems were adequate and operating effectively

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28



Definitions – KMP [Section 2(51)]

Key Managerial Personnel [Section 2(51)] (Notified on 12th September, 2013) - in relation to a company, means

- ☐ The CEO or the MD or the manager
- ☐ Company Secretary
- ☐ Whole – time Director
- ☐ CFO
- ☐ Any other prescribed officer

As per AS – 18:

KMP means those persons who have the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise

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30

Related Party Transactions

What does the Companies Act, 1956 say ? [Section 297 (1)]

- Central government approval required for entering into specific contracts, where paid-up capital of the company is not less than Rs.1 crore; for other Companies – the Board approval where interested Directors are not to participate
- Following transactions are covered:
 - Sale, purchase or supply of any goods, material or services
 - Underwriting the subscription of any shares or debentures
- Sale/purchase of goods/services for cash at prevailing market prices not exceeding Rs 5K – are exempted
- No specific disclosure required in the Board Report

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31

Related Party Transaction (notified)

➤ **Sec 2(76)** -Related party with reference to a company, means:

- (i) a director or his relative;
- (ii) a **key managerial personnel** or his relative;
- (iii) a firm, in which a director, **manager** or his relative is a partner; (**CFO and CS also covered**)
- (iv) a private co. in which a director or **manager** is a member or director;
- (v) a public co. in which a director or **manager** is a director or holds **along with his relatives**, more than 2% of its paid-up S/C;
- (vi) any body corporate whose BoD, M.D or manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager;
- (vii) any person on whose advice, directions or instructions a director or manager is accustomed to act: **Provided that nothing in sub-clauses (vi) and (vii) shall apply to the advice, directions or instructions given in a professional capacity;**
- (viii) any company which is—
 - (A) a holding, subsidiary or an associate company of such company; or
 - (B) a subsidiary of a holding company to which it is also a subsidiary (fellow subsidiary)
- (ix) such other person as may be prescribed – director or KMP of holding company and their relatives

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32

Related Party Transaction

1956 Act	2013 Act
<ul style="list-style-type: none"> Limited scope of transactions and persons covered under Co Act (S. 297) Prior approval of CG required in case paid-up capital exceeds INR 10 million (INR 1 crore) 	<ul style="list-style-type: none"> Enhanced scope of transactions Enhanced scope of related parties to include KMP and relatives, directors with certain shareholding, persons in advisory capacity (other than professional advice) to board Prior approval of shareholders by SR if: <ul style="list-style-type: none"> paid-up capital exceeds Rs 10 Cr Trx exceeding higher of 25% of T/O or 10% of N/W as per last audited FS Appointment exceeding Remuneration of Rs 2.5 Lac pm Underwriting remuneration etc exceeding 1% of networth No member shall vote if he is related party

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33

Related Party Transactions ...cont'd

Following transactions are covered u/s 188

- sale, purchase or supply of any goods or materials;
- selling or otherwise disposing of, or buying, property of any kind;
- leasing of property of any kind;
- availing or rendering of any services;
- appointment of any agent for purchase or sale of goods, materials, services or property;
- such related party's appointment to any office or place of profit in the company, its subsidiary company or associate company; and **(Rs 2.5 Lakh per month or more)**
- underwriting the subscription of any securities or derivatives thereof, of the company (remuneration not **more than 1% of networth**)

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34

Related Party Transactionscont'd

Provisions of Sec 188 of New Act—Sub Rule 15 of Chapter XIII.

- Prior Board Approval – Board meeting agenda to contain details like name of related party, nature of relationship, contract details, manner of determining pricing and commercial terms, if certain factors not considered then rationale for not considering , etc.
- Prior approval by SR at GM required if paid-up capital of Co is Rs.10 Cr or more **OR** the transaction with RP does **not** exceed such sum, as may be prescribed (The word “not” is mis-placed in Section).
 - For sale or purchase of goods or material -- exceeding 25% of annual turnover
 - Selling, buying or leasing of property or availing or rendering of services --- exceeding 10% of net worth
- Interested member not to vote on SR – **(issue for some Co's)**
- Disclosure in board report along with justification for RPT
- Section exempts: Any transaction entered by company in its ordinary course of business other than transactions which are not an arm's length basis
- NOTE – For wholly owned subsidiaries (**WOS**), special resolution is sufficient for transactions with Holding company

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35

“Related Parties”- Defined Term

Related Parties	2013 Act	1956 act
KMP or his relative	Yes	No
Senior Management of the Co. (All members of management 1 level below the executive directors, including the functional heads)- as per rules	Yes	No
A firm in which such director, manager or relative is a partner	Yes	Some changes
Public co. in which a director or manager is a director	Yes	No
Holding, subsidiary , fellow sub. or an associate co. along with their directors & relatives, their KMPs & relatives, their Senior management	Yes	No

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36

“Related Parties”- Defined Term

Related Parties	2013 Act	1956 act
Public co. in which a director or manager is a Director holds along with his relatives, > 2% of its paid-up S/C	Yes	Some changes
Any person on whose advice, directions or instructions a director or manager is accustomed to act, unless advice is given in a professional capacity	Yes	Some changes
Body corporate whose BoD's, MD or manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager unless advice is given in a professional capacity	Yes	Some changes

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37

Section 2(77) Rule					
Change in Definition - (Relative)					
	Act 2013	Act 1956		Act 2013	Act 1956
Members and HUF	Y	Y	Husband and wife	Y	Y
Father (including step-father)	Y	Y	Mother (including step-mother)	Y	Y
Father's father	N	Y	Mother's father	N	Y
Father's mother	N	Y	Mother's mother	N	Y
Son (including step-son)	Y	Y	Daughter (NOT MENTIONED including step-daughter)	Y	Y
Son's wife	Y	Y	Daughter's husband	Y	Y
Son's son/ daughter	N	Y	Daughter's son daughter	N	Y
Son's son's wife	N	Y	Daughter's son's wife	N	Y
Son's daughter's husband	N	Y	Daughter's daughter's husband	N	Y
Brother	Y	Y	Sister	Y	Y

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38

Loan to Directors



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39

Exemptions etc... Withdrawn....

Loan etc to Directors Etc... (**Notified on 12th September 2013**)

- | | | |
|----------|---|---|
| Sec. 295 | { | <ul style="list-style-type: none"> • Applicable only to Public Co.'s • Now Applicable to Private Co.'s also |
| Sec. 185 | | |

The company cannot give loan to :

- Any Director of lending Co or of Holding Co
- Any **partner or relative** of any such Director
- Any firm in which any such **Director or relative** is partner
- Any PVT Co of which any such Director is Director or Member
- Any Body Corporate of which **25%** or more of total voting power is exercised/**controlled** by any such Director(s)
- Any Body Corporate the BoD or MD or manager whereof is accustomed to act in accordance with directions /instructions of BoD or of any Director(s) of lending co.

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40

Exemptions etc... Withdrawn....

- S. 295 of Old Act exempted Pvt. Ltd Co.'s; but the New Act does not
- Further, prohibited loans/guarantees can be made with the approval of CG under the Old Act; In the New Act there is no such provision of CG permission
- Loans/Guarantees & Securities from holding co. to/in favor of subsidiary not exempted by Section.

However, Rule has given such an exemption.

Draft notification u/s 462 dated June 24, 2014- 185 Shall not apply to Pvt co.'s -

(a) which have borrowings from banks or FI's or any bodies corporate not more than twice of their paid up S/C or Rs. 50 crore, whichever is lower; &

(b) in whose S/C no other body corporate has invested any money

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41

Exemptions etc... Withdrawn.... Cont'd

- Exemptions given under Rule 10(1) – Chapter XII
 - a) Loan by Holding Co. to **Wholly Owned Subsidiary (WOS)** or guarantee or security provided by a holding company in respect of **any loan** made to its **WOS** is exempted
 - b) Rule 10 (2) Any guarantee given or security provided by a holding company in respect of loan made by **any bank or FI** to its **subsidiary company** is exempted
 - c) Provided loans made under 10 (1) & (2) are utilised by subsidiary for its principle business activities.
- Only exceptions in Sec 185:
 - ✓ loan given to MD or WTD if such loan is in accordance with the terms of services extended to all employees or is approved by shareholders by SR
 - ✓ Loans etc. given in ordinary course of its business **(conditions apply)**

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42

Exemptions etc... Withdrawn.... Cont'd

Consequences of non-compliance:

- ✓ Fine to Company - Rs 5 Lakh to Rs 25 Lakh
- ✓ Fine to Director or borrower - Rs 5 Lakh to Rs 25 Lakh or Imprisonment upto Six months or Both

Unlike in Sec. 295, the exemption from imprisonment, if loan is repaid fully, is not there in Sec. 185

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43

S. 185 – Discussion in Select Committee Pg 67;

Suggestion	Comments of Ministry
This clause corresponds to section 295 of existing Act. However, section 295(2) seems to have been inadvertently overlooked. Such exemption is necessary. A holding and subsidiary company are in substance one entity and consolidated financials ensure that all their transactions with third parties are accounted and disclosed. Consequently, it is necessary to give freedom to companies to deal with their subsidiaries as if they are mere divisions of the company.	The Irani Committee on new Company Law (2005) had made following recommendations in connection with restrictions for loans to be made to directors :- —5.1 Generally the directors should not be encouraged to avail of loans or guarantees from companies. They should be allowed remuneration or sitting fees only. <u>In case company decides so, loans to directors should be allowed only when company by special resolution approves such loans. Disclosures to be made to shareholders, through the explanatory statement, should be specified in the rules.</u> It should be open to a company to formulate schemes (such as Housing Loan Schemes) for the benefit of Executive Directors. Once such schemes are approved by the shareholders by special resolution, loans under such schemes may be allowed to eligible directors, without again going to shareholders for approval. // (b) The provisions proposed in the Companies Bill, 2011 are in accordance with above recommendation and were similarly included in the Companies Bill, 2009.

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44

Restrictions on Inter- Company Loan and Investments (Draft notification u/s 462 dated June 24,2014- Section 188 RPT not applicable to pvt co.'s)



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45

Exemptions etc... Withdrawn.... Cont'd

➤ Intercompany Investments and Loans

- Sec. 372A { • Applicable only to Public Co.'s
- Sec. 186 { • Now Applicable to Private Co.'s also

Changes:

- **Exemption in case of loan by Holding Co to WOS also withdrawn in section S.372A** was regulating **only inter-corporate loans/investments** but S. 186 in New Act **applies to Loan etc to any person??**
- **Now under Rule 11 of Chapter XII**
Loan or guarantee given or security provided by Holding Co. to **Wholly Owned Subsidiary Co.** or JV or acquisition of securities of Wholly Owned Subsidiary (**WOS**) --Prior S.R. Not Required
- Under the old Act, no loan shall be given at a ROI **lower than the prevailing bank rate** being the standard rate made public under section 49 of the Reserve Bank of India Act, 1934
- Under the New Act, no loan to be given at a ROI < the **prevailing yield of 1 year, 3 year, 5 year, or 10 year G-Sec closest to the tenor of the loan**

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46

Exemptions etc... Withdrawn.... Cont'd

- **Additional disclosure in financial statements-** full particulars of the loans given, investment made or guarantee given or security provided and the purpose for which the loan or guarantee or security is proposed to be utilized by the recipient of the loan or guarantee or security
- 186(1) Restriction on layers of, Investment subsidiaries to two layers except for subsidiaries outside India or if required by law
- 186 (2)- No company shall directly or indirectly — **(No change)**
 - (a) give any loan to any person or other body corporate;
 - (b) give any guarantee or provide security in connection with a loan to any other body corporate or person; and
 - (c) acquire by way of subscription, purchase or otherwise, the securities of any other body corporate, exceeding 60% of its paid-up S/C, free reserves and S.P account or 100% of its free reserves and S.P account, whichever is more

If exceeds the limits then prior approval by S.R in G.M shall be necessary
- **Exemptions-**
 - Loan, guarantee or security by banking companies, insurance companies, housing finance companies, companies in the business of financing of companies, companies **providing infrastructural facilities**
 - Acquisition of Security by a co./ NBFC whose principal business is acquiring securities

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47

Subsidiaries & Associates



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48

Subsidiary Company-Section 2(87)-notified

- **Subsidiary company** in relation to any other company (that is to say the holding company), means a company in which the holding company—
 - (i) controls the composition of the Board of Directors; or
 - (ii) exercises or controls more than **one-half of the total share capital** either at its own or together with one or more of its subsidiary companies:
- The term 'subsidiary company' has been defined with reference to words "**total share capital**" instead of "**total voting power**"
- **Rule 2(r) for Section 2(6) & 2(87) Total Share Capital means Paid up Share Capital + Convertible Preference Share Capital**

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49

Subsidiary Company-Section 2(87)

- **Subsidiary shall include associate and joint venture**
- **2(87):** Provided that such class or classes of holding companies as may be prescribed **shall not have layers of subsidiaries beyond** such numbers as may be **prescribed (rules are silent)**
- **Section 186(1)** restricts **layers of Investment Subsidiary** up to **2 except** in case of:
 - a company from acquiring any other company incorporated in a country outside India if such other company has investment subsidiaries beyond 2 layers as per the laws of such country
 - a subsidiary co. from having any investment subsidiary for the purposes of meeting the requirements under any law or under any rule or regulation framed under any law for the time being in force

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50

Associate Company - Section 2(6) - notified

- Associate Company means a company in which other company has significant influence and is not a subsidiary of other company and includes JV
- Significant influence means control of at least 20% of total S/C, or of business decisions under an agreement
- The term 'Associate Company .' is defined to include 'joint venture' also & both terms also refer to '**Total Share Capital**' instead of '**Voting Power**'
- Further vide explanation to section 129(3) it is provided that for purpose of '**consolidation**' the word '**subsidiary**' shall include '**an Associate**' or '**JV**'

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51

Associate Company - Section 2(6) - notified

- AS-23 makes holding of 20% or more of voting power as rebuttable presumption that company is an 'Associate'
- The combined reading of these provisions give rise to conflict as to consolidation of '**Associate**' & '**JV**' & **manner thereof**
- However, the rule 9.4 attempts to remove the ambiguity w.r.t. to Consolidation and clarifies that **Consolidation of FS shall be made in accordance with the Accounting Standards**

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52

Restrictions on Acceptance of Deposit

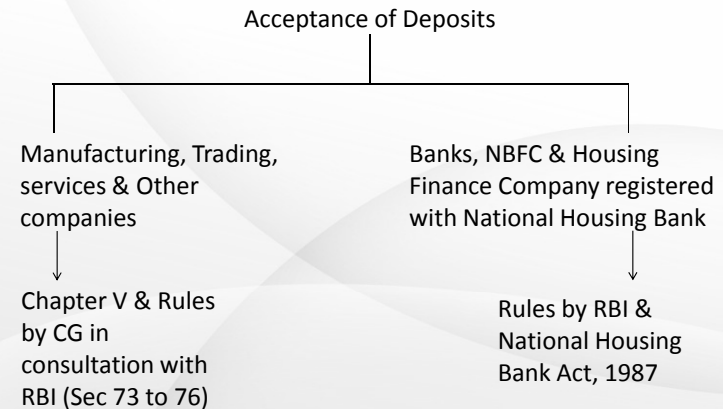


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53

Acceptance of Deposits



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Acceptance of Deposits [Chapter V Companies (Acceptance of Deposit) Rules, 2014]

1. Amounts from directors will not amount to deposit provided declaration that amount is not being given from borrowed funds
2. Deposit from any other Company can be accepted
3. amount brought in by the promoters of the company on the stipulation of any lending financial institution or a bank
4. **All Companies (other than Eligible Company)** from members can accept deposit up to 25% of paid up share capital & free reserves
- Co.'s can (including private Co.'s excluding banks & NBFC) subject to **the passing of resolution** in GM & such rules **as may be prescribed** in consultation with the RBI accept deposits **from its members** if the following conditions are fulfilled:
 - ✓ Issuance of circular to members containing financial position, credit rating, details of past deposits still not repaid & other particulars

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55

Acceptance of Deposits

- ✓ Files copy of circular with ROC in 30 days
 - ✓ maintenance of 15% liquid deposits on Deposits maturing during the year & next year
 - ✓ deposit insurance- < Rs 20000, full amount, > Rs 20000, not less than Rs 20000
 - ✓ Details of security, if any proposed to be given
 - ✓ Appointing one or more deposit trustees in case of Secured Deposits—Rules of Appointment & duties
 - ✓ Certify that the co. has not defaulted in repayment of deposits
5. **Eligible Company**
- Criteria for Eligible company Public Company - N/W ≥ 100 cr, T/O ≥ 500 cr, Prior Consent in GM by SR filed with ROC / RBI as the case may be

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56

Acceptance of Deposits

Conditions:-

- Deposit from members should not exceed 10% of paid up share capital and free reserves
- Other Deposits should not exceed 25% of paid up share capital and free reserves
- Issue advertisement in Newspapers
- If inviting Public Deposit shall upload a copy of the circular on its website, if any
- **government companies**, deposit should not exceed 35% of paid up share capital and free reserves
- Interest rate or brokerage for all deposits from members by eligible company not to exceed the rule prescribed by RBI for NBFC

Acceptance of Deposits

Section 76- Public Company can accept deposits if: a

- compliance with section 73(2) i.e. circular & rules framed by CG in consultation with RBI
- Credit rating of at least "adequate safety" and set it every year
- Incase of secured deposits create charge or assets to the extent of deposit accepted within 30 days

Transitional provision for repayment of existing deposit (Sec. 74)

- File Statement with ROC in 3 months containing details of Deposit unpaid, interest payable, & arrangements for repayment
 - Repayment within 1 year or maturity whichever is earlier & statements of O/s deposits to be filed with RoC within 3 months)
 - Tribunal can give further time for repayment

Acceptance of Deposits... Cont'd

- Deposit will include, inter alia, as per rules:
 - a) Share application money outstanding beyond 60 days and such application money/ advance is not refunded within 15 days
 - b) advances received for supply of goods or provision of services outstanding beyond 365 days
 - c) advances from buyers of immovable property provided advance is adjusted against property.
- If (b) & (c) refundable due to lack of approvals, then it is to be considered as deposit.

Acceptance of Deposits... Cont'd

Punishment

On failure to repay the deposit or part thereof or any interest thereon within the time specified:

- Repayment of deposit and interest
- Fine not less than Rs 1crore which may extend to Rs 10 crore
- Officer in default -imprisonment which may extend to seven years or fine not less than Rs 25 lacs to Rs 2 crores, **or with both**

Damages for fraud- Deposit accepted with intend to defraud depositors:

- Officer responsible to be personally liable, without any limitation of liability for all the losses or damages incurred by the depositor

ACCOUNTS OF THE COMPANY

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Companies Act, 2013

61

Definitions – Financial Statements [Section 2(40)]- notified

Balance Sheet

P&L Account OR
Income &
Expenditure
Account

Cash Flow Statement

Statement of
changes in equity, if
applicableAny other
explanatory note

“Financial Statements” include ‘cash flow statement’ in case of all companies except ‘OPC’ and ‘Small Companies’ as against the provisions of AS-3 which applies only to SMC’s

Included in Financial Statements

	Act 2013	Act 1956
SFS	Schedule III	Schedule VI
CFS	As per Schedule III applicable to the Comp <u>Additional Discourses</u>	Not specified

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62

Turnover

Section 2(91)

- **Turnover** means the **aggregate value of the realization of amount** made from the sale, supply or distribution of goods or on account of services
- Reference to the other sections (eg.)
 - Sec 2(85) : Small Company
 - Sec 76 : Acceptance of deposits from public
 - Sec 135 : Corporate Social Responsibility

- Whether adjustment needed for opening and closing trial balances
- Any impact on preparation of financial statements

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63

Consolidated Financial Statements (CFS)

- **What were the provisions of the Companies Act, 1956 w.r.t to CFS ?**
 - No Provision
- **What does the Listing Agreement say ? (Clause no. 41)**
 - Holding Co. **may** submit quarterly and year to date consolidated financial results to the stock exchanges
 - It is **mandatory** for the Holding Co. to submit **annual audited** consolidated financial results/statements to the stock exchanges
- **What does the Companies Act, 2013 say?(Sec129)**
 - Holding Co. to prepare CFS in addition to Stand alone financials
 - Earlier such requirement for only listed company, now it is applicable to **all (private or public) if they have any subsidiary company**
 - Moreover, Subsidiary is defined to include Associate and Joint Venture for the purpose of CFS

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64

CFS....cont'd

- CFS to be prepared by the Holding Co. in the same form and manner, as that of its own

Issues:

- Different GAAPs followed in foreign subsidiaries
- Different reporting formats followed in (i) foreign subsidiaries, (ii) different sectors, e.g. insurance banking etc..
- **CFS** to be circulated to members & shall **also be laid before A.G.M.** of the Holding Co. Therefore, Auditor's report on CFS will have to be addressed to members. Currently clause 32 of Listing Agreement required listed companies to prepare and publish CFS but same was not required to be laid before AGM for approval
- Proviso to Section 129(3)-**Holding Co.** to attach with its **financial statement**, a separate statement containing the salient features of the financial statement of its subsidiaries, in to be prescribed form

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65

CFS....cont'd

- The Act does not contain any provision which corresponds to provisions of Section 212 of the 1956 Act and it appears that details required to be given in respect of subsidiary co.'s **u/s 212 are dispensed with**
- Old section 212 required attachment of FS, BoD's report, auditor's report, statement of holding co.'s interest in subsidiary company. Unlike section 212 there **is no requirement** for reporting developments during period comprising different accounting years and **no reporting** on non-availability of information
- *Schedule III (earlier Sch VI) contains separate "general instructions" in relation to CFS and requires disclosure of a statement of particulars to be given as part of CFS*
- *Minority Interest in CFS Balance Sheet to be shown separately from Equity of Parents*

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66

CFS....cont'd

In Consolidated Financial Statements, the following shall be disclosed by way of additional information:

Name of the Entity in the	Net Assets i.e. total assets minus total liabilities		Share in profit or loss	
	As % of Consolidated net assets	Amount	As % of Consolidated profit or loss	Amount
Parent				
Subsidiaries				
Indian				
Foreign				
Minority Interest in all Subsidiaries				
Associates (Investment as per the equity method)				
Indian				
Foreign				
Joint Venture (as per proportionate consolidation/ investment as per the equity method)				
Indian				
Foreign				

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67

CFS....cont'd

- For the first time, Consolidated Financial Statements (CFS) are accorded recognition under Corporate Law; in fact, where a company has subsidiary and/or joint venture and/or an associate, the Act provides for mandatory preparation of CFS
- Section 136 is drafted in manner to require every company whether listed or not, but having subsidiary/ies to place on their website, if any separate audited accounts of subsidiary
- All Companies (whether listed or unlisted and whether public or private) having subsidiary or Associate or JV would have to prepare and present CFS
- Management and auditors of Private & Unlisted Public Companies need to gear up to meet this requirements of CFS

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68

Section 2(87)

Holding – Subsidiary Company

		Equity Shares (Voting)	Convertible Preference Shares	Total
Total Share Capital of X Ltd. (all FV Rs. 10)	Nos.	10,000	5,000	15,000
Investments by Y Ltd. in Share Capital of X Ltd. (all FV Rs. 10)	Nos.	6,000	500	6,500
% of Ownership		60.00%	10.00%	43.33%

	Act 2013	AS 21
Whether X Ltd. is subsidiary of Y Ltd.	No	Yes

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69

Financial Year

Section 2(41)

Particulars	Act 2013	Act 1956
Financial Year	<ul style="list-style-type: none"> Period ending 31st March of the year Transitional period of 2 years for existing companies Applicable to all companies except foreign holding or subsidiary companies which requires – <ol style="list-style-type: none"> Compulsory consolidation outside India; and With prior approval of Tribunal 	Period for which profit & Loss account placed before AGM
FY Period (except 1 st FY of incorporation)	<ul style="list-style-type: none"> 12 months Can not be less or more than 12 months 	<ul style="list-style-type: none"> Normally it cannot exceed 15 months Can extend it to 18 months, after getting permission from the registrar

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70

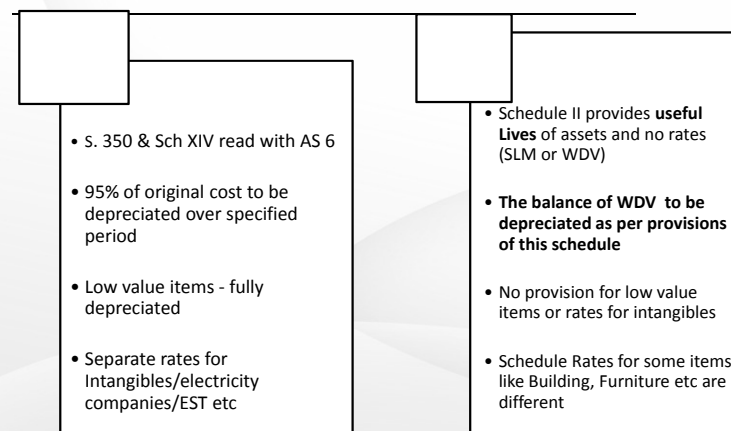
Maintenance & Preservation of Books of Accounts

- What does the Companies Act 1956 say ? (Section 209)
 - The Act is silent on maintenance of accounts in electronic form
 - Preservation of accounts were required for a period not less than 8 years immediately preceding the current year
- What does the Companies Act, 2013 say ? (Section 128)-
 - The Act seeks to permit maintenance of accounts in electronic form
 - The Act provides where investigation is ordered in respect of a company, the Central Government may direct that accounts may be kept for such longer period as it thinks fit. (Otherwise 8 years)
- The other provisions pertaining to (i) maintenance of accounts under accrual method (ii) Description of Books of Account (iii) Format of disclosure of FS [Schedule III – earlier Schedule VI] etc have been, more or less, retained in same manner

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71

Depreciation

Carrying value of FA to be depreciated over the remaining revised useful life of the asset

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72

Depreciation

Some significant Changes:

Asset	Rate of Depreciation-1956 Act	Rate converted to years-1956 Act	Useful Life-2013 Act	Longer life/ (Shorter life)
Continuous Process Plant	5.28	18	25	7
General Plant & Machinery	4.75	20	15	(5)
General Rate for furniture & fittings	6.33	15	10	(5)
Electrically Operated Vehicles	7	13.57	8	(5.57)
Computer	16.21	5.86	3	(2.86)
Furniture & fittings used in hotels etc...	9.5	10	8	(2)

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73

Depreciation

Some significant Changes:

Asset	Rate of Depreciation-1956 Act	Rate converted to years-1956 Act	Useful Life-2013 Act	Longer life/ (Shorter life)
Building (other than factory building) other than RCC frame structure)	1.63	61.35	30.00	(31.35)
Bridges	1.63	61.35	30.00	(31.35)

• If useful life or residual value is different for Schedule II, Justification to be disclosed

- Component accounting under Note 4
- Extra Shift depreciation higher – 50%
- Triple Shift - 100%

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74

Schedule II

Amortization – Intangible Assets

- Act 2013
 - Depreciation includes amortization [Part A(2) to the schedule II of the Act, 2013]
 - Pre Revised Schedule II - *Amortization as per AS 26* except Toll Road under BOOT or BOT or other form of PPP where revenue based amortization is permitted as explained.

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75

DEPRECIATION /AMORTIZATION

Schedule II

DEPRECIABLE AMOUNT OF AN ASSET

- **ACT 1956:**
- DEPRECIATION TO BE PROVIDED ON THE BASIS OF HISTORIC COST, BEFORE DECLARATION OF DIVIDEND AND MANAGERIAL RENUMERATION
- **ACT 2013:**
- DEPRECIABLE AMOUNT IS THE COST OF AN ASSET, OR OTHER AMOUNT SUBSTITUTED FOR COST, LESS RESIDUAL VALUE [NOTE 5 TO PART C OF SCHEDULE II]
- ICAI GN ON "TREATMENT OF RESERVES CREATED ON REVALUATION OF FIXED ASSETS"

Issues :

- Whether GN is still applicable?
- Amount standing to the credit of Revaluation Reserve

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76

Schedule II

Depreciation / Amortization

	Act 2013	Act 1956
Useful Life	<ul style="list-style-type: none"> Tangible Assets: Useful Life of assets based on class of components Intangible Assets : As per AS Transactional Provisions 	<ul style="list-style-type: none"> 95% of cost to be depreciated at the rates specified in Schedule XIV (SLM or WDV) AS 6
UoP Method	Allowed	Not allowed (MCA Circular)
Depreciable Amount	Cost or amount substituted for cost	Cost
Component Accounting	Mandatory	Optional
Extra Shift	Separate rates not prescribed Double Shift : Increase by 50% Triple Shift : Increase by 100%	Separate rates specified
Assets less than Rs. 5,000	No specific requirement	100%

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77

DEPRECIATION / AMORTISATION**Component Accounting**

Schedule II

- ACT 2013
- 1. WHERE COST OF ANY PART OF THE ASSET IS SIGNIFICANT TO THE TOTAL COST OF THE ASSET AND USEFUL LIFE OF THAT PART IS DIFFERENT FROM THE USEFUL LIFE OF THE REMAINING ASSET, USEFUL LIFE OF THAT SIGNIFICANT PART TO BE DETERMINED SEPARATELY
- PARA 8.3 OF AS 10- OPTION TO FOLLOW
- SIGNIFICANT CHANGE IN ACCOUNTING FOR REPLACEMENT COST.

Issues :

- Prescribed useful life for the whole assets then how component accounting will work for class C companies to the Schedule II
- Identification of significant component cost thereof
- Assets capitalized before enactment of Act 2013, core part is now due for replacement

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78

Schedule II

Depreciation / Amortization**Transitional Provision**

- Note 7, Part C, Schedule II
"From the date this schedule comes into effect, the carrying amount of the assets as on that date –
(a) Shall be depreciated over the useful life of the assets according to the Act, 2013
(b) after retaining the residual value, shall be recognized in the opening balance of retained earnings where the remaining life is nil"
- No transitional provisions
- Examples

Useful Life (Years)		Actually used (Years)	Treatment of remaining carrying value
Schedule XIV (1956)	Schedule II (2013)		
58	30	30	Retained Earning
58	30	29	<ul style="list-style-type: none"> Statement of Profit & Loss Impact on EPS

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79

Free Reserves & Net worth - notified

- Section 2(43):** Reserves which are as per the latest audited balance sheet of a company available for distribution as dividend

Following shall not be treated as free reserve:

- any amount representing unrealized gains, notional gains or revaluation of assets, whether shown as a reserve or otherwise, or
 - any change in carrying amount of an asset or of a liability recognized in equity, including surplus in profit and loss account on measurement of the asset or the liability at fair value
- Section 2(57):** net worth means the aggregate value of the paid-up S/C and all reserves created out of the profits and S.P. account, after deducting the aggregate value of the accumulated losses, deferred expenditure & miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation

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80

SEC 2(43) FREE RESERVES

Section 2(43)

- REFERENCE TO OTHER SECTIONS:
- SEC 63 – ISSUE OF BONUS SHARES
- SEC 68 – BUY BACK OF SHARES
- SEC 69 – TRANSFER TO CRR
- SEC123 – DECLARATION OF DIVIDEND
- SEC 180 – BORROWING POWER LIMIT
- SEC186 – LOANS AND INVESTMENTS

Whether adjustment needed for :

- AS 11 – Gain accounted on restatement
- AS 15 – Fair Value of plan assets
- AS 19 – Initial Recognition of assets taken on financial assets
- AS 26 – Recording of an intangible asset, acquired in exchange for shares or other securities, at fair value

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81

Bonus Share-Revaluation Reserve

- Earlier, no provision on issue of bonus shares by Companies except Table A mentions about capitalization of profits and reserves; but it does not specially prohibit capitalization of revaluation reserve
- Listed entities- SEBI regulates issue of Bonus shares
- Guidance note issued by ICAI- company is not permitted to issue bonus shares out of revaluation reserve
- In Bhagwati Developers Vs peerless General finance and Investment Co. (2005), SC held that and unlisted company can issue bonus share out of revaluation reserve

Act 2013

- Section 63 - A company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of—
 - (i) its free reserves;
 - (ii) the securities premium account; or
 - (iii) the capital redemption reserve account:

Provided that no issue of bonus shares shall be made by capitalizing reserves created by the revaluation of assets

Rule 4.12 - A company cannot subsequently withdraw the decision of board recommending issues of bonus shares

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82

Bonus Shares (Section 63)

Pre-condition for issue of Bonus share - No company shall capitalize its profits or reserves for the purpose of issuing fully paid-up bonus shares, unless—

it is authorized by its articles;
it has, on the recommendation of the Board, been authorized in the general meeting of the company;
it <u>has not defaulted in payment of interest or principal</u> in respect of <u>fixed deposits or debt securities</u> issued by it;
it has not defaulted in respect of <u>the payment of statutory dues of the employees</u> , such as, <u>contribution to provident fund, gratuity and bonus</u> ;
the partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up;
it complies with <u>such conditions as may be prescribed</u>
bonus shares <u>shall not be issued in lieu of dividend</u>

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83

Section 52(2) & (3)

Utilization of Securities Premium

	Act 2013		Act 1956
	Prescribed class of Companies(not yet prescribed)	Others	
Issue of fully paid equity shares as bonus shares	Y	Y	Y
Issue of fully paid preference shares as bonus shares	N	Y	Y
Writing off preliminary expenses	N	Y	Y
Writing off the expenses of, or the commission paid or discount allowed on			
• Equity Shares	Y	Y	Y
• Preference Shares	N	Y	Y
• Debentures	N	Y	Y

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84

Utilization of Securities Premium

	Act 2013		Act 1956
	Prescribed Class of Companies	Other	
Providing for premium payable on redemption of			
• Preference Shares	N	Y	Y
• Debentures	N	Y	Y
Buy-back of its own			
• Securities	-	-	Y [Sec 77(1)]
• Shares or other specified securities	Y	Y	

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Companies Act, 2013

85

Reopening / Revision of Accounts

What does the Companies Act, 1956 say ?

- No specific provision relating to reopen the accounts of the company

What does the Companies Act, 2013 say? (Section 130 & 131)-

- A company shall re-open its books of account and recast its financial statements, only if an application in this regard is made by the Central Government, the Income-tax authorities, the Securities and Exchange Board, any other statutory regulatory body or authority or any person concerned and an order is made by a court of competent jurisdiction or the Tribunal to the effect that—

- (i) the relevant earlier accounts were prepared in a fraudulent manner;
- or
- (ii) the affairs of the company were mismanaged during the relevant period, casting a doubt on the reliability of financial statements

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Companies Act, 2013

86

Reopening /Revision of Accounts.... Cont'd

- The court or the Tribunal, as the case may be, shall give notice to the C.G, the IT authorities, the SEBI or any other statutory regulatory body or authority concerned and shall take into consideration the representations, if any, made by that Government or the authorities, Securities and Exchange Board or the body or authority concerned before passing any order under this section
- The accounts so re-casted or revised shall be final
- Section 131 provides that it is also possible for the BoD to revise the financial statements or Board's report for any of the 3 previous financial years if they find that the statement and / or the report is not in accordance with the requirement of Section 129 or 134
- The Board will seek approval of Tribunal for the same and before giving approval the tribunal shall give notice to **the Government and the Income tax Department** and invite their comments

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87

Reopening of Accounts / Revision.... Cont'd

- Authorities such as SEBI, RBI, IRDA etc have not been mentioned in the Act
- Such revision can be made only once in a financial year
- The board shall give the detailed reasons for revision to the members and send revised copies to members and RoC. The revised financial statements shall be approved by members in general meeting
- Strict interpretation of the new provision would, mean that any revision/ reopening of F.S. would now, solely, be permitted through a court/ Tribunal driven process, wherein an application to this effect would need to be filed by either one of the specific classes of applicants mentioned and that too limited to the earlier discussed 2 grounds
- No time-limit prescribed for reopening and revising the accounts or FS consequent to Court or tribunal order

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Companies Act, 2013

88

Section 130
and 131

Re-Opening and Revision

	Re-opening of Accounts	Revision of Financial Statements
Coverage	Accounts	FS and BR
Application by	CG, IT Authority, SEBI, or other statutory body or authority or any person concerned	By directors [Rules by BOD]
Period	Not specified	3 preceding financial years
Order/ Approval by	Tribunal or Court of competent jurisdiction	Tribunal
Triggering Events	<ul style="list-style-type: none"> Accounts were prepared in fraudulent manner Doubt on reliability of FS due to mismanagement 	Non Compliance related to: <ul style="list-style-type: none"> SFS and CFS (Sec. 129) Board Report (Sec. 134)

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Companies Act, 2013

89

Section 130 and
131

Re-opening and Revision

Rules

- Majority directors or auditors have changed
 - Company shall disclose such facts in the application
 - Tribunal will issue notice and hear such auditor
- General Meeting to be called in which summarized statement of revision effected, Copy of Tribunal Order, Revised FS, Statement of Directors and auditors, Revised auditor's report on the revised FS placed for consideration and adoption of revised FS.
- The revision shall be reported upon by the auditor who is presently holding the position of auditor.
- The proposed revision shall be presented to the directors and auditors who authenticated the original FS and reports.
- Revised FS or report of the Board shall be signed as required u/s 134

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90

DEBENTURES

Section 2(30)

- ACT 2013**
- DEBENTURES INCLUDE DEBENTURE STOCK, BONDS OR ANY OTHER INSTRUMENT OF COMPANY EVIDENCING A DEBT, WHETHER CONSTITUTING CHARGE ON ASSETS OF COMPANY OR NOT
- CREATION OF DRR OUT OF PROFITS OF THE COMPANY AVAILABLE FOR PAYMENT OF DIVIDEND AND THE AMOUNT CREDITED TO SUCH ACCOUNT TO BE UTILIZED ONLY FOR REDEMPTION OF DEBENTURES
- ACT 1956 [SEC 2(12)]**
- "DEBENTURE" INCLUDES DEBENTURE STOCK, BONDS AND ANY OTHER SECURITIES OF A COMPANY, WHETHER CONSTITUTING A CHARGE ON THE ASSETS OF THE COMPANY OR NOT

Whether ICD would be treated Debentures? If yes, Debenture Redemption Reserve [Sec 71(4)]?

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91

AUDIT & AUDITORS



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92

Definitions - Auditing Standards - 2(7)

- **Auditing Standards** means the standards of auditing or any addendum thereto for companies or class of companies referred to in Clause 143 (10);

(Clause 143(10) - The CG may prescribe the standards of auditing or any addendum thereto, as recommended by the ICAI, in consultation with and after examination of the recommendations made by the National Financial Reporting Authority)

- The Standards on Auditing (SA) formulated by ICAI are in sync with International Standards on Auditing (ISA) with minor differences. The SA to be formed or recommended by NFRA may also need to be on the lines of best international practices
- Appropriate documentation evidencing the work done & procedures (planning, control testing, substantive & analytical etc.) performed, review, QC & visibility of process leading to conclusion culminating in Audit Report, Management Letter, ACP etc. will be required to establish the compliance of auditing standards

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93

Appointment of Auditors

- Where a co. is required to constitute an AC under section 177, all appointments, including the filling of a casual vacancy of an auditor under this section shall be made after taking into account the recommendations of such committee
- Before appointment of auditor u/s 139(1), as per the proviso to rule 3.1, the audit committee, or the Board if there is no audit committee, shall consider the order or pending proceedings relating to professional matter of conduct against the proposed auditor before the Institute of Chartered Accountants of India or competent authority or any Court

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Companies Act, 2013

94

Rotation of Auditors

- **What does the Companies Act, 1956 say ?**

➤ No provision relating to rotation of auditors

- **What does the Companies Act, 2013 say ? [Section 139(2)]**

- Listed company and all **other companies**** excluding OPC and small co.'s
- a) an individual as auditor for more **than 1 term of 5 consecutive years**; and
 - b) an audit firm as auditor for more than **2 terms of 5 consecutive years**

****Other Companies:**

- (a) unlisted public companies having paid up share capital of rupees 10 crore or more;
- (b) private limited companies having paid up share capital of rupees 20 crore or more;
- (c) companies having paid up share capital of below threshold limit mentioned in (a) and (b) above, but having public borrowings from financial institutions, banks or public deposits of rupees 50 crores or more

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95

Rotation of Auditors

Provided that—

- (i) an individual auditor who has completed his term of 5 years, **not to be re-appointed as auditor** in the same co for 5 years from the completion of his term
- (ii) an audit firm which has completed its 2 terms of 5 years, **not to be re-appointed** as auditor in the same company for 5 years from the completion of such term

Provided further that as on the date of appointment **no audit firm:**

- (a) having a common partner or partners to the other audit firm;
- (b) whose tenure has expired in a co. in the immediately preceding the financial year;
- (c) **shall not be appointed as auditor of the same company for a period of 5 years**

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96

Rotation of Auditors

2nd Proviso to Section 139(2)- Existing companies have to comply with the requirements within 3 years from the date of commencement of the Act

- Rules clarifies that, in case of an auditor (whether an individual or audit firm), the period for which he or it has been holding office as auditor prior to the commencement of the Act shall be taken into account in calculating the period of five consecutive years or ten consecutive years, as the case may be

Qualifications of Auditors

➤ Section 141(3)(d) prohibits a person to be eligible for appointment as auditor if:-

- ✓ Person/Partner is holding any security of or interest in the co. or its subsidiary, or of its holding or associate co. or a subsidiary of such holding co.

A relative of such person or of Partner may hold securities of face value or interest in the co. not exceeding **Rs 1000** or such higher amount as may be prescribed [Rule 10.7(1) prescribes limit of upto **Rs. 1lac**]

- ✓ Person/Relative/Partner is indebted / has given a guarantee or provided any security in connection with the indebtedness of any third person, or its subsidiary, to the co. or its holding or associate co. or a subsidiary of such holding co., **except person or relative or partner** who as per rule 10.7(2)(3), are exempted upto **Rs. 5lakh** for indebtedness and upto **Rs. 1 lakh** for guarantee/security

Disqualification

(Securities or Interest / Indebtedness / Guarantee or Security)

Section 141(3)(d)
Rule 10 of
chapter 10 Rules

Hold Security or Interest in Co.
FV exceeding Rs. 1 lakh

A Person or his
relative or partner

Indebted to
Co. / Subsidiary / Holding /
Associate / Fellow Subsidiaries
in excess of Rs. 5 lakhs

Guarantee / Security of Third person
in excess of Rs.1 lakhs

In the company

- To the company ; or
- Its subsidiary or holding; or associate company ;or
- A subsidiary of such holding company

**Subsidiary of
associate
company not
covered**

Disqualification as auditor

In case of Securities - Auditors / Partners / cannot hold any security

Appointment of Internal Auditor

- By every Listed Co.
- By every Unlisted Public Co. & Private Company having

Particulars	Unlisted Public Company	Private Company
Paid up Share Capital	≥ 50 Crores	N.A.
Turnover	≥ 200 Crores	≥ 200 Crores
Outstanding loans or borrowings from banks or PFI	≥ 100 Crores	≥ 100 Crores
Outstanding Deposit	≥ 25 Crores	N.A.

Additional grounds for disqualification

- a person whose relative is a director or is in the employment of the co. as a director or KMP
- a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of **more than 20 co.'s**

Draft notification u/s 462 dated June 24,2014- pvt co not to be counted for limit

- person who has been convicted by a court of an offence involving fraud and a period of 10 years has not elapsed from the date of such conviction
- **141 (3) (i) any person whose subsidiary or associate company or any other form of entity, is engaged as on the date of appointment in consulting and specialised services as provided in section 144**

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101

Duties of Auditor – Internal Control & Fraud

▪ What does the Companies Act, 1956 say ? (Section 227)

- CARO required to report on internal control matter relating to the inventory, fixed assets and sale of goods and services
- CARO required to report of any fraud on or by the company has been noticed or reported during the year

▪ What does the Companies Act, 2013 say ? (Section 143)

- Auditor shall report that company has **adequate internal financial controls system in place** and the **operating effectiveness** of such controls
- If an auditor of a company, in the course of the performance of his duties as auditor, has reason to believe that an offence involving **fraud is being or has been committed against the company** by officers or employees of the company, he shall report the matter to the CG -

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102

Duties of Auditor – Internal Control & Fraud

- ✓ within **30** days of his knowledge or information, with a copy to the audit committee or in case the company has not constituted an audit committee, to the Board
- ✓ **The report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed post followed by an email in confirmation of the same**
- ✓ **The report shall be on the letter-head of the Auditor and be signed by the Auditor with his seal and shall indicate his Membership Number**
- ✓ The report shall be in the form of a statement as given in Form No. 10.3
- Whether auditor has **sought and received** the information/explanations which he considers necessary for the purpose of audit

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103

Penal Provisions

Violation by Auditor		Fine/ Imprisonment			
Section	Description	Sections	Imprisonment	Minimum (Rs.)	Maximum (Rs.)
140(2)	On resignation by auditor, he needs to intimate company and ROC or CAG	140(3)	-	0.5 Lakh	5 lakh
141(3)	Disqualifications of auditors	141(4)	Vacation of office		
143(12)	Reporting on fraud	143(15)	-	1 Lakh	25 Lakh

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104

Penal Provisions

Violation by Auditor		Fine/ Imprisonment		
Section	Description	Sections	Unknowingly	Knowingly/ Willfully with intention to deceive
139	Appointment of auditor	147(2) and 147(3)	<ul style="list-style-type: none"> Minimum Rs. 25000 Maximum Rs. 5 Lac 	<ul style="list-style-type: none"> Imprisonment upto 1 year; and Minimum fine Rs. 1 lac Maximum fine Rs. 5 lac
143	Power and duties of auditor			
144	Auditor not to render certain service			
145	Auditor to sign audit report			

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105

Matters to be stated in Audit Report

- As per section 143(3) read with rule 10.8, the auditor report shall also include their views and comments on the following matters-
 - whether, in his opinion, the F.S. comply with the AS
 - observations or comments on financial transactions or matters having adverse effect on the functioning of the co.
 - whether any director is disqualified from being appointed as a director u/s 164(2)
 - any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith
 - Whether co. has adequate internal financial controls system and the operating effectiveness of such controls
 - **The effect of pending litigations on its financial position**
 - **Provision for foreseeable losses, on long term contracts including derivative contracts**
 - Delay in depositing money into IEP Fund

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106

Removal of Auditors

- **What does the Companies Act 1956 say? [Section 224 (5)]**
 - At a general meeting company can remove the auditors by passing a special resolution and after obtaining approval from the central government
- **What does the Companies Act, 2013 say (Section 140)**
 - CG approval and SR required to remove auditor before his term
 - The tribunal either suo motu or on an application by C.G or by any other concerned person, if satisfied that the auditor of a co. has, directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the co. or its directors or officers, it may, by order, direct the co. to change its auditors and the auditor shall not be eligible to be appointed as an auditor of any company for a period of 5 years from the date of passing of the order

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107

Resignation of Auditors

- **What does the Companies Act, 1956 say ?**
 - No provision of filling any document with ROC on resignation
- **What does the Companies Act, 2013 say ? (Section 140)**
 - The auditor who has resigned from the company shall file within a period of 30 days from the date of resignation, a statement in **Form no 10.2** with the company and the Registrar, and in case of Government companies and Government controlled companies, the auditor shall **also** file such statement with the C&AG, **indicating the reasons and other facts as may be relevant with regard to his resignation**
 - If the auditor does not comply with the above requirement, he or it shall be punishable with fine which shall not be less than Rs.50,000 but which may extend to Rs.5,00,000

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108

One Person Company





Small Company & Dormant Company

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109

One Person Company [Section 2(61)]

- Which has only 1 person as a member
- Minimum 1 director
- Sec 3(1)(c) – only private company can be formed
- Perpetual Succession through Nomination
- Paid up Capital ≤ Rs. 50 Lakhs & Turnover ≤ Rs. 2 Crore

New vehicle with limited liability to enter into Corporate framework

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110

One Person Company

Definition:

One Person Company (Section 2 (62)) - means a company which has only one person as a Member

What is a One Person Company?

As the name suggests, it means a company which has only one person as a member and where legal and financial liability is limited to the company only and not to that person (i.e. liability is limited)

Benefits & Other provisions

1. FS - Cash flow statement not required
2. Nominee Clause in MOA - to maintain perpetual succession
3. Annual Returns to be signed by CS, or where there is no CS, by a director
4. Need not hold AGM

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111

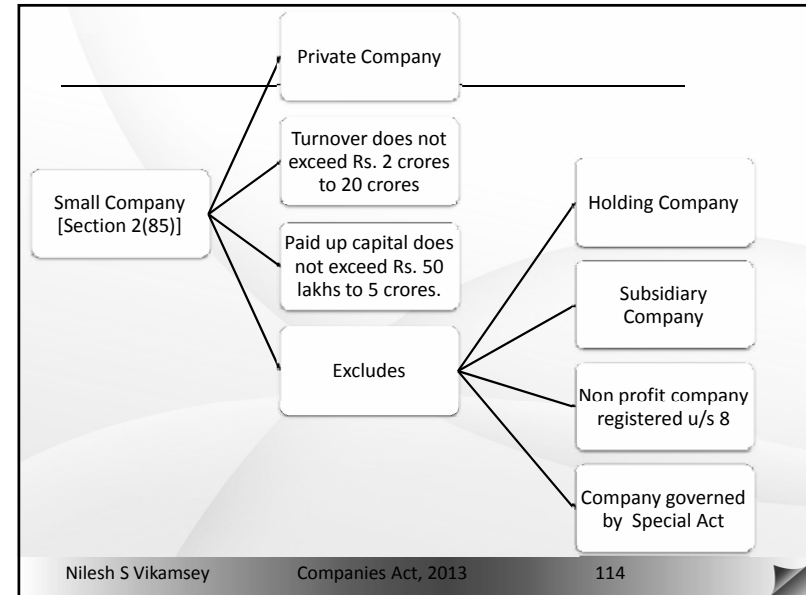
Benefits & Other provisions for OPC

5. Inform ROC about every contract entered and recorded in the BOD's meeting minutes within 15 days of approval by BOD
6. Any business required to be done at AGM/GM by OR or SR, only member to communicate to Co. and be entered in the minutes-book, signed and dated by member
7. In case of one Director on the board any business which is required to be done at BOD meeting, just enter the resolution of such director in the minutes-book and signed and dated by such director
8. OPC shall be mentioned in brackets below the name of such company, wherever its name is printed, affixed or engraved

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112

Benefits & Other provisions Cont'd

9. File copy of FS adopted by member, along with all related documents, within 180 days from close of financial year
10. Individual deemed to be 1st director until directors are duly appointed by the member
11. If there are more than one director hold at least 1 meeting of the BOD's in each half of a calendar year with a **min** gap of 90 days b/w both meetings.
12. Terms of contract entered (except in ordinary course of business) by OPC limited by shares /guarantee with the sole member of the company who is also the director of the company, shall, except when it is in writing, be contained in a MOA or are recorded in the minutes of the 1st meeting of the BOD's held next after entering into contract



Small Company

➤ **Small Company (Section 2 (85))** - means a company, other than a public company,—

- i. paid-up share capital of which does not exceed Rs.50 lacs or such higher amount as may be prescribed which shall not be more than Rs.5 crore or
- ii. turnover of which as per its last profit and loss account does not exceed Rs.2 crores or such higher amount as may be prescribed which shall not be more than Rs.20 crore

Provided that nothing in this clause shall apply to—

- a) A holding company or a subsidiary company;
- b) A company registered with Charitable Objects; or
- c) A company or body corporate governed by any special Act;

Small Company.... Cont'd

Privileges/exemptions to small Company:

1. Financial Statements need not include cash flow statement
2. Annual Returns of Small company can be signed by the CS or where there is no CS, by any director of the company (CS in practice not required in such cases)
3. Clause 173 requires Small Company to hold at least 1 meeting of the BOD's in each half of a calendar year with a min gap of 90 days b/w both meetings
4. The Company Act introduced a simplified procedure for merger & amalgamation between two small companies without approval of tribunal, subject to compliance with certain other procedures

Small Company.... Cont'd

Sr. No	Basis	Companies Act, 2013	Companies (Accounting Standards) Rules, 2006	CARO (Amend) 2004
1	Nomenclature	Small Company	SMC's	Private Ltd Co.
2	Applicability	Private Company	Both public or private	Private Ltd Co.
3	Paid up share Capital	<=50 lakhs or such higher amount as prescribed (Max 5 cr)	N.A.	<=50 lakhs (including reserve)
4	Turnover	<= 2 Crore or such higher amount as may be prescribed (Max 20 crore)	<=50 crore	<=5 crore
5	Borrowings	N.A.	<= 10 cr in last year	<= 25 lacs from any bank or FIS

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117

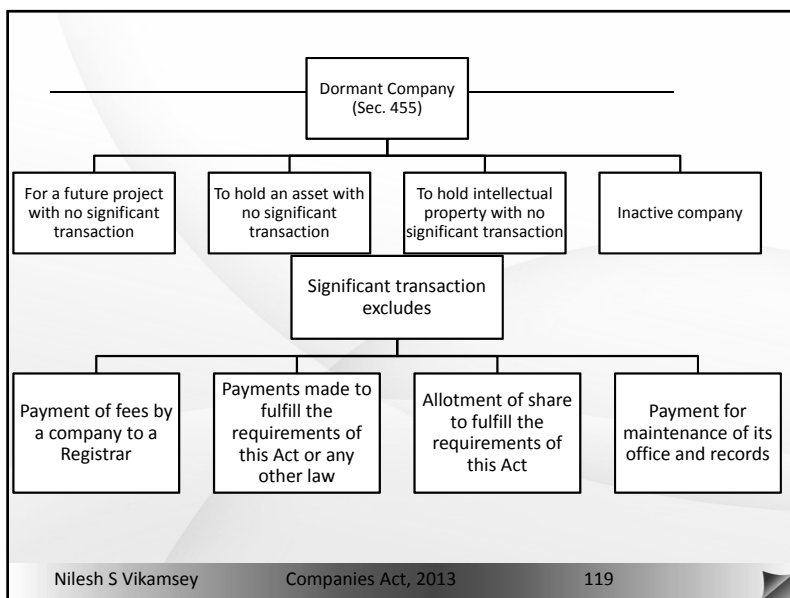
In following situations whether small company / SMC is required to prepare Cash Flow Statement?

	Details	Rs. In Cr.	Act 2013	AS
I	Paid-up Capital	0.40	Not Required	Not Required
	Turnover	1.50		
II	Paid-up Capital	0.60	Required	Not Required
	Turnover	1.50		
III	Paid-up Capital	0.40	Not Required	Required
	Turnover	11.00		

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118



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119

Dormant Company

Section/Rule	Particulars	Description
Section 2 (40)	financial statement – Cash Flow Statement not required	the financial statement, with respect to One Person Company, small company and dormant company, may not include the cash flow statement
Sec 173 (5)	Frequency of Board Meeting in a calendar year	A One Person Company, small company and dormant company shall be deemed to have complied with the provisions of this section if at least one meeting of the Board of Directors has been conducted in each half of a calendar year and the gap between the two meetings is not less than ninety days:
Rule 29.8	Minimum number of directors for dormant company	a dormant company shall have a minimum number of <u>three directors</u> in case of a public company, two directors in case of a private company and one director in case of a One Person Company

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120

Dormant Company

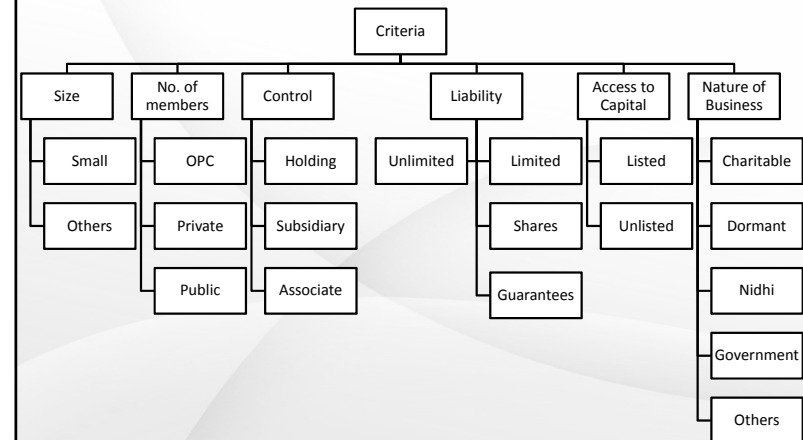
Section/Rule	Particulars	Description
Rule 29.8(Proviso)	Retirement of Directors by rotation	the provisions of the Act in relation to the rotation of directors shall not apply on dormant companies
Rule 29.9	Return of dormant companies	a dormant company shall file a declaration annually in Form No. 29.4 along with such annual fee as provided within thirty days from the end of each financial year
Proviso to Rule 29.9	No relaxation in filing Return of Allotment	The Dormant Company Shall continue to file the return(s) of allotment in the manner and within the time specified in the Act whenever the company allots any security to any person

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121

Classification of Companies



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122

LTD

VS

LLP

LTD vs LLP

Area	Company	LLP
Law regulated under:	Companies Act, 2013 (which has replaced the old Companies Act, 1956 w.e.f. 29.08.2013)	LLP Act, 2008
Minimum Capital requirement	1 Lakh for Pvt Ltd.	No such requirement
Income Tax	Profits of the Indian Company will be taxable @ 32.445% (inclusive of Surcharge & cess)	Profits will be taxed in the hands of the LLP @ 30.90% (inclusive of cess).
Dividend Distribution Tax	The Indian Company will be subject to Dividend Distribution Tax @ 16.995% (inclusive of surcharge and cess) as per Indian Tax laws	Dividend Distribution Tax not applicable for profits distributed by a LLP
CSR	Applicable to all companies having limits specified under section 135 of companies Act 2013	No such provisions

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124

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123

LTD vs LLP

Area	Company	LLP
Compliances at the time of Formation	<ul style="list-style-type: none"> Registration with ROC by making necessary applications Report to RBI within 30 days of receipt of subscription money / share application money into India Report to RBI within 180 days of allotment of shares against subscription money / share application money into India 	<ul style="list-style-type: none"> Registration with ROC required No filing requirements prescribed as of now by RBI Approval from FIPB for foreign ownership.
Limited Liability	Liability is limited only to the share capital held in Indian company	Liability of Partners is limited to the extent of their agreed contribution towards LLP except in case of intentional fraud or wrongful act of omission or commission by the partner, where, errant partner will be liable.
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LTD vs LLP

Area	Company	LLP
Minimum number of shareholders / directors / partners / agents	Minimum 2 & maximum 200 Shareholders Minimum 2 Directors The Company should have atleast 1 director to be resident who has stayed in India for a period of 182 days in a previous calendar year.	Minimum 2 partners. Designated Partner (DP) – The LLP should have atleast 2 individuals as DPs. One of them has to be a person resident in India. The DP would be responsible for compliance of LLP and FEMA laws by the LLP.
Cost Of Formation	Comparatively high	Comparatively Low
BOD Report	BOD required to give detailed report	No Such Requirements
Audit Committee	Required to form an Audit Committee	No Such Requirements
Loan To Directors	Prohibition on Loans and Advances under Section 185 & 186	No Such Requirements

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126

LTD vs LLP

Area	Company	LLP
Rotation of Auditors	Applicable to all companies except Small companies and OPC	No such restrictions
Compliances	Substantial level of Compliance	Lower Level of Compliance
Related Party	Restriction on Related party transaction	No such restriction
Acceptance of Deposit	Stringent condition for acceptance of deposit by any company	No such restriction (subject to RBI Act)
Class Section Suit	Class Section Suit could be filed against company	No such provision in LLP Act

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127

Draft notification u/s 462 dated June 24,2014

Other sections from which private co.'s are exempted-

1. Sec 160- Right of person other than retiring Director to stand for Directorship
2. Sec. 162- Appointment of Directors to be voted individually
3. Sec 180 - Restrictions on power of Board, Shall not apply to private companies having 50 or less number of members
4. Sec 203 (3) Appointment of KMP

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128

