



MCA proposes amendments to the Companies Act, 2013

21 November 2018

First Notes on

Financial reporting
Corporate law updates
 Regulatory and other information
 Disclosures

Sector

All
 Banking and insurance
 Information, communication, entertainment
 Consumer and industrial markets
 Infrastructure and government

Relevant to

All
 Audit committee
 CFO
 Others

Transition

Immediately
 Within the next three months
 Post three months but within six months
 Post six months

Forthcoming requirement

Introduction

The MCA considered certain amendments to the Companies Act, 2013 (2013 Act) while deliberating the recommendations made by the Report of the Committee to review Offences under the Companies Act, 2013 (the report).

This issue of First Notes provides an overview of key amendments proposed by Ministry of Corporate Affairs (MCA).

The proposals are in respect with the following provisions:



Overview of the proposed amendments

The table below provides an overview of the key proposals

Appointment and qualification of directors

<p>Company to have Board of Directors (Section 149)</p>	<p>Pecuniary relationship</p> <p><i>Current guidance:</i> In relation to criteria pertaining to the independent director, currently the 2013 Act requires that an independent director should not have any pecuniary relationship, other than remuneration as a director or have a transaction not exceeding 10 per cent of his/her total income or such amount as may be prescribed, with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year.</p> <p><i>Proposal:</i> A cap on threshold for total pecuniary relationship has been proposed. The proposal mentions that pecuniary relationship with the company, its holding, subsidiary or associate company, or their promoters, or directors, should not exceed 25 per cent of director's total income. Out of 25 per cent of total income, professional or any services rendered by him/her, other than prescribed services, should not account for more than 10 per cent of his/her total income.</p> <p>The remuneration received¹ and expenses incurred for participation in the meetings of Board of Directors and other meetings would not be accounted for determining the total pecuniary relationship, unless otherwise provided.</p> <p>Every independent director is required to complete an assessment, conducted by a body or an institute, as may be prescribed. However, the central government Government may, by order, exempt an individual or any class of individuals from the requirement of completing such an assessment.</p> <p>Declaration</p> <p><i>Current guidance:</i> Currently under 2013 Act, every independent director is required to provide a declaration that he/she meets the criteria of independence, in the first meeting of the Board of Directors in which he/she participates as a director and thereafter at the first meeting of the Board of Directors in every financial year or whenever there is any change in the circumstances which may affect his/her status as an independent director.</p> <p><i>Proposal:</i> An independent director to also file a return with the Registrar of Companies (ROC), containing such particulars of his/her independence, as may be prescribed.</p>
<p>Resignation of Director (Section 168)</p>	<p><i>Proposals:</i> A director (other than an independent director) may forward a copy of his/her resignation along with detailed reasons for the resignation to the ROC within 30 days of resignation in such manner as may be prescribed.</p> <p>Every independent director would be required to forward a copy of his/her resignation along with detailed reasons for the resignation to the ROC within seven days of giving notice of his/her resignation under Section 168, in such form and manner as may be prescribed.</p> <p>The resignation of an independent director would take effect on the thirtieth day from the date of receipt of notice by the company (as mentioned above) or such later date as may have been specified in the said notice.</p>
<p>Removal of Directors (Section 169)</p>	<p><i>Current guidance:</i> Currently under 2013 Act, the company can remove those independent directors that were re-appointed for second term under Section 149 by passing a special resolution and after giving him/her a reasonable opportunity of being heard.</p> <p><i>Proposal:</i> Any independent director can be removed by a company by passing a special resolution and after giving him/her a reasonable opportunity of being heard.</p>

¹As per Section 197, *Overall Maximum Managerial Remuneration and Managerial Remuneration in Case of Absence or Inadequacy of Profits* of the 2013 Act

Accounts of companies

Constitution of National Financial Reporting Authority (Section 132)

Proposal: The MCA proposes following additional provisions to facilitate effective constitution of National Financial Reporting Authority (NFRA)

- The NFRA would be permitted to constitute divisions as may be prescribed to perform its functions
- Each division of the NFRA would be presided over by the chairperson or a full-time member authorised by the chairperson
- There would be an executive body of NFRA consisting of the chairperson and full-time members for the efficient discharge of functions of the NFRA.

Corporate Social Responsibility (Section 135)

Current guidance: Currently under the 2013 Act, every company is required to spend at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility (CSR) policy.

Proposal: For a company which has not completed the period of three financial years since its incorporation, such a company would compute two per cent of the average net profits for such period computed since its incorporation.

Any amount remaining unspent would be transferred by a company within 30 days from the end of the financial year to a special account to be opened by the company for that financial year in any scheduled bank to be called the Unspent CSR Account. This amount would be spent by the company in pursuance of its CSR policy within a period of three financial years from the date of its transfer.

The central government may give such general or special directions to a company or class of companies as it considers necessary to ensure compliance of provisions of Section 135 and such company or class of companies would comply with such directions.

Prevention of oppression and mismanagement

Application to Tribunal for Relief in Cases of Oppression, etc. (Section 241)

Current guidance: If in the opinion of the central government the affairs of the company are being conducted in a manner prejudicial to public interest, it may itself apply to the Tribunal (National Company Law Tribunal (NCLT)) for an order under prevention of oppression and mismanagement provisions.

Proposals: The application to NCLT in respect of a company or class of companies (where affairs of the company are being conducted in a manner prejudicial to public interest), as may be prescribed, would be made before the Principal Bench of the NCLT.

The central government may state a case against the person in specified scenarios and refer the same to the NCLT with a request that the NCLT may inquire into the case and record a decision as to whether or not such a person is a fit and proper person to hold the office of director or any other office connected with the conduct and management of any company. The specified scenarios are:

- a) Any person concerned in the conduct and management of the affairs of a company is or has been in connection therewith guilty of fraud, misfeasance, persistent negligence or default in carrying out his/her obligations and functions under the law, or breach of trust
- b) The business of a company is not or has not been conducted and managed by such person in accordance with sound business principles or prudent commercial practices
- c) A company is or has been conducted and managed by such a person in a manner which is likely to cause, or has caused, serious injury or damage to the interest of the trade, industry or business to which such a company pertains or
- d) The business of a company is or has been conducted and managed by such a person with intent to defraud its creditors, members or any other person or otherwise for a fraudulent or unlawful purpose or in a manner prejudicial to public interest,

Additionally every application to NCLT should contain following:

- A concise statement of such circumstances and materials as the central government may consider necessary for the purpose of the inquiry, and
- Signed and verified in the manner laid down in the Code of Civil Procedure, 1908, for the signature and verification of a plaint in a suit by the central government.

Prevention of Oppression and Mismanagement (cont.)

Powers of Tribunal (Section 242)	<p><i>Proposal:</i> At the conclusion of the hearing of the case in respect of Section 241(3), the NCLT should record its decision in an order stating therein specifically as to whether or not the respondent is a fit and proper person to hold the office of director or any other office connected with the conduct and management of any company.</p>
Consequence of Termination or Modification of Certain Agreements (Section 243)	<p><i>Proposals:</i></p> <ul style="list-style-type: none"> • The person against whom an order has been made under Section 242(4A), he/she should not hold the office of a director or any other office connected with the conduct and management of the affairs of any company for a period of five years from the date of the said order. Further, the central government may, with the leave of the NCLT, permit such a person to hold any such office before the expiry of five years. • Notwithstanding anything contained in any other provision of 2013 Act, or any other law for the time being in force or any contract, memorandum or articles, on the removal of a person from the office of a director or, as the case may be, any other office connected with the conduct and management of the affairs of the company, that person would not be entitled to, or be paid, any compensation for the loss or termination of office.

Others

Formation of Companies with Charitable Objects, etc. (Section 8)	<p><i>Proposal:</i> A company registered under Section 8 (i.e. with charitable objects) would not be allowed to convert itself into a company of any other kind.</p>
Register of significant beneficial owners in a company (Section 90)	<p><i>Proposal:</i> The proposal enhances management responsibility to identify an individual who is a significant beneficial owner. Every company would need to take all necessary steps to find out if there is any individual who is a significant beneficial owner in relation to the company and if so, to identify him and require him to comply with the provisions of Section 90.</p>
Unpaid Dividend Account (Section 124)	<p><i>Current guidance:</i> Currently under 2013 Act, the provision relating to transfer of funds to Investor Education and Protection Fund (IEPF) provides that the 'all shares in respect of which dividend has not been paid or claimed for seven consecutive years or more shall be transferred by the company in the name of IEPF along with a statement containing such details as may be prescribed'.</p> <p><i>Proposal:</i> The proposal now requires that the transfer should be made along with any dividend, which has not been paid or claimed, in such shares, together with interest, if any, accrued thereon in the name of IEPF.</p>
Merger or Amalgamation of Certain Companies (Section 233)	<p><i>Current guidance:</i> Currently the 2013 Act provides that the provisions of Section 233 should apply mutatis mutandis to a company or companies specified in respect of a scheme of compromise or arrangement referred to in section 230 (Power to Compromise or Make Arrangements with Creditors and Members) or division or transfer of a company referred Section 232 (Merger and Amalgamation of Companies) of the 2013 Act.</p> <p><i>Proposal:</i> The MCA replaces the above provision and proposes that the central government may make rules for allowing compromise or arrangement in respect of any company specified under Section 233(1), and</p> <ul style="list-style-type: none"> • Its creditors or any class of them, or • Its members or any class of them, or • Any other company specified therein.

Our comments

The Ministry of law and justice with the aim of promoting ease of doing business and ensuring better corporate governance notified the Companies (Amendment) Ordinance, 2018 (the ordinance). The ordinance has been issued considering the recommendations made by the Report of the Committee to review Offences under the Companies Act, 2013 (the report). The amendments incorporated under the ordinance are effective from 2 November 2018.

Further, while drafting the amendments incorporated under the ordinance, the MCA considered certain other amendments to strengthen the corporate governance and enforcement framework. Accordingly, MCA has recently released proposals for amendment to the 2013 Act for stakeholders' consideration.

Some of the key proposals are:

- **Independent director:** Following are four new provisions proposed to the 2013 Act:
 - **Pecuniary relationship of an independent director:** Under the Companies Amendment Act, 2017, MCA had amended the Section 149 with regard to pecuniary relationship of an independent director. It mentions that pecuniary relationship will not include remuneration of a director or a transaction not exceeding 10 per cent of his/her total income (or such amount as may be prescribed), with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year. This amendment did not mention any cap on the amount of remuneration that an independent director could charge a company, its holding, subsidiary or associate company, or their promoters, or directors but does put a cap on the other kind of transactions upto 10 per cent of the total income of the independent director.
 Now MCA proposes to impose a cap on computation of total pecuniary relationship (including remuneration) of an independent director with the company, its holding, subsidiary or associate company, or their promoters, or directors, i.e. it should not exceed 25 per cent of his/her total income.
 Out of this 25 per cent, an independent director would be able to charge for professional or any services rendered by him upto a maximum of 10 per cent of his/her total income. Therefore, the proposal is to limit the payments for other services or professional fees upto 10 per cent of the total income.
 It is important to note that the above limit of 25 per cent of the total income of an independent director would not include the sitting fees and expenses incurred for participation in the meeting of board and committees.
 - **Declaration by an independent director:** The MCA aligns the provision with regard to independence of independent director with the SEBI Listing Regulations. Under Listing Regulations the board is required to provide for confirmation in corporate governance section of the annual report that the independent director satisfies the requirement for independence and is independent of management. On the same lines, the MCA proposes that such independent director should file return with the ROC, containing such particulars of his/her independence, as may be prescribed.
 - **Resignation:** The MCA proposes new provisions relating to resignation by an independent director and align the same with the Listing Regulations. Under Listing Regulations, listed entities within seven days of resignation independent director are required to disclose to the stock exchange detailed reasons for the resignation. The MCA now proposes that such resigning independent director should forward a copy of his/her resignation along with detailed reasons for the resignation to the ROC within seven days of giving notice of his/her resignation. However, other directors would have an option to forward the resignation to the ROC.
 - **Removal of directors:** The proposals aim to relax the procedure to remove an independent director from a board. The current requirements of the 2013 Act allow removal of an independent director when he/she is in the second term. The proposal mentions that an independent director can be removed by a company by passing special resolution at any time of his/her tenure.
- **CSR:** The MCA clarifies that companies which have not completed the period of three financial years since their incorporation would be required to make CSR spend of two per cent of the average net profits for period computed since its incorporation.

Further, a company that has not been able to spend the entire CSR amount in a financial year, then the amount remaining unspent would be required to be transferred to a special bank account in a scheduled bank within 30 days from the end of the financial year. The company would be required to spend this amount in accordance with its CSR policy within three financial years from the date of transfer of funds. This proposal raises an issue whether the transfer of funds to a special bank account would trigger the requirement to make a provision in the financial statements in accordance with Ind AS 37, *Provisions, Contingent Liabilities and Contingent Assets* (or AS 29) for the unspent CSR amount. In the past, the Institute of Chartered Accountants of India had issued a Guidance Note on Accounting for Expenditure on CSR Activities, on 15 May 2015 which clarified that a provision in the financial statements is not required when there is a shortfall in spending on CSR activities in relation to the prescribed limits. The companies should consider this issue.

Additionally, the central government proposes to give itself powers to issue directions to a company or a class of companies to ensure compliance with the provisions of Section 135.

Our comments (cont.)

- **Government can make an application to NCLT against certain individuals:** Apart from making an application to NCLT when the affairs of a company are being conducted in a manner prejudicial to public interest, the central government proposes to make an application to NCLT against certain individuals in certain scenarios. Those scenarios could be a situation of fraud, misfeasance, persistent negligence or default, business of a company is not or has not been conducted and managed by such person in accordance with sound business principles or prudent commercial practices, business of a company is or has been conducted and managed by such person with intent to defraud its creditors, members or any other person or otherwise for a fraudulent or unlawful purpose or in a manner prejudicial to public interest, etc.
- **NFRA:** The MCA proposes certain provisions relating to constitution of divisions under NFRA to ensure effective constitution of NFRA.
- **Others:** There are certain other provisions proposed relating to Section 8 companies, significant beneficial owner, merger or amalgamation of certain companies, etc. to ensure effective framework for companies.

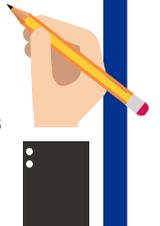
On the whole, this is a welcome development and is expected to establish an effective corporate governance framework for the companies.

The bottom line

The proposal to amend 2013 Act represents MCA's continuing effort to align the 2013 Act with SEBI Listing Regulations and enforcement of effective corporate governance for the Indian companies.

The MCA is moving the needle of governance by imposing a cap on remuneration to independent directors, requirement to file declaration, etc.

Further, the proposal on CSR is also an important development as it seeks to impact practice of companies that were not spending on CSR expense. The proposed amendment would result in some adjustment to companies CSR programs as well as working capital requirements.



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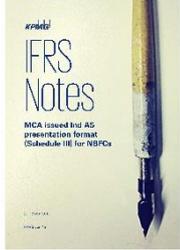
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MCA issued Ind AS presentation format (Schedule III) for NBFCs

26 October 2018

On 11 October 2018, MCA through its notification has amended Schedule III to the 2013 Act. The amendments, inter alia, have incorporated a new division to Schedule III i.e. Division III which provides general instructions for presentation of financial statements of an NBFC1.

The amendments to Schedule III are applicable from 11 October 2018.

This issue of IFRS Notes provides an overview of the key changes made to Division I and II and also highlights the key requirements of Division III (applicable to NBFCs) to Schedule III of the 2013 Act.

Missed an issue of Accounting and Auditing Update or First Notes



Issue no. 27 – October 2018

The topics covered in this issue are:

- Ind-AS 115 – What does it mean for consumer market and retail sectors?
- Revision in auditing of accounting estimates
- Measurement of investments under separate financial statements
- Regulatory updates



ICAI clarifies applicability of disclosure norms relating to Specified Bank Notes (SBNs)

4 September 2018

On 1 September 2018, the Institute of Chartered Accountants of India (ICAI) through an announcement clarified that the above disclosure requirements relating to SBNs (in the notes to account as well as in the auditor's report) are not applicable for the FY2017-18 and subsequent years. Accordingly, consequent disclosures may be given in the financial statements/auditor's reports.



Voices on Reporting

KPMG in India is pleased to present **Voices on Reporting** – a series of knowledge sharing calls to discuss current and emerging issues relating to financial reporting.

In a special session held on 19 November 2018, we discussed significant impact areas of Ind AS 115, *Revenue from Contracts with Customers* and Ind AS 103, *Business Combinations* on technology sector.

Click here to access the [audio recording](#) (mp3) and [presentation](#) (pdf).

Feedback/queries can be sent to aaupdate@kpmg.com

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