Companies Act 2013

Action has begun

February 2014
Agenda

1. Where are we
2. Board Disclosures
3. Related Party Transactions
4. Key Messages
5. Q&A
Section

Where are we
Where are we

- Passed by both houses of parliament and received the assent of the President.
- Currently, 98 sections of the Companies have been notified; both the acts i.e. Companies Act, 1956 and Companies Act 2013 Act co-exist
- Draft rules and forms have been released for public comments.
- Companies Act 2013 expected to be fully notified by March 2014 along with the issuance of all the related Rules / Forms
A statistical snapshot

- In more than 73% of sections, the government has the power to prescribe rules
- Executive can get into legislative domain

<table>
<thead>
<tr>
<th><strong>Companies Act, 2013: A Statistical Snapshot</strong></th>
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<tbody>
<tr>
<td><strong>Number of Schedules</strong></td>
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<tr>
<td><strong>Number of Chapters</strong></td>
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<tr>
<td><strong>Number of times the phrase ‘as may be prescribed’ is used</strong></td>
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<tr>
<td><strong>Number of Sections</strong></td>
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Section

Key highlights and analysis

2
Directors – Interesting New Concepts

1. Resident Director
2. Can not be a director in more than 10 public cos
3. Alternate Director
4. Continued absence could lead to vacation
5. Reasons of resignation
6. Duty towards community

• Ambiguity laid to rest in case of alternate directors
New disclosures mandated in directors’ report

1. Risk management policy

2. Adequate Process to ensure legal compliance and its operating effectiveness

3. Corporate Social Responsibility

4. Board Evaluation

5. Operating effectiveness of Internal Financial Controls*

6. Related party contracts with their justification

- Good to have things have been made must have
- Applicable for listed cos
**Board’s Confirmation on compliance**

1. Inventory of applicable laws & compliance obligations
2. Responsible persons for compliance
3. Compliance Reporting through Chief Compliance Officer
4. No red flags or non compliances in high risk category
Board’s Confirmation on RPT

1. List of related parties

2. Transactions in ordinary course of business

3. Arms length Pricing

4. Approvals
Role of a Company Secretary

1. Report to the board about compliance with the provisions of the act
2. Report to the board about compliance with other laws applicable to the company
3. To ensure that company complies with applicable secretarial standards meeting
4. To provide guidance to the directors of the company on their duties and responsibilities
5. To discharge such other duties as may be prescribed

Company Secretary to report to the board on other applicable laws as well
Every Listed company and every other company with paid up share capital of 5cr or more to have following full-time KMPs:

(i) The Chief Executive Officer or the managing director or the manager or WTD,

(ii) The company secretary,

(iii) The Chief Financial Officer

- Can a KMP be appointed as a KMP in any other company?
- What all documents can be signed by KMP?
- Covered in definition of related party
Officer in Default – Opportunities to delegate

1. Whole-Time director/Key Managerial Personnel
2. Director or Directors specified by the Board
3. Any person with the authority of Board/KMP, responsible for maintenance / filing of records or accounts etc fails to take preventive steps
4. Registrar / Merchant Bankers - issue / transfer of securities
Immunity to non-executive and independent directors

Limited immunity not available in case of:

- Lack of due diligence
- Knowledge and consent or connivance

- Limited immunity in specified circumstances
Related Party Transactions: New concepts

1. ‘Related Party’ and ‘Transactions’ expanded
2. No need for Central Government approval
3. Concept of interested member
4. Approval by majority of minority
5. Role of Independent Directors, Audit Committee, Company Secretary
Related Party Transactions

- Scope of transactions widened – includes sale or purchase of any property
- Need for Central Government approval done away with
- Shareholder’s approval for specified transactions
- Concept of interested member:
  - Member can not vote if it is a related party
  - Exemption for contracts between Holding and WoS
- Routine transaction at ‘Arm’s length’ exempted
- RPTs to be included in the Board’s Report along with justification
‘Related Party’ means:

- A director or his relative
- A firm in which a director or his relative is a partner
- A private in which a director is a member or director
- A public co in which a director along with relatives hold more than 2% of paid up capital
- Any body corporate whose board is accustomed to act – instructions of a director
- A KMP or his relative
- Holding co/Subsidiary co / Associate co
- Subsidiary of a holding company
- Such other person as may be described
Scope of transactions widened

- Transactions covered:
  - Sale, purchase or supply of goods or materials
  - Selling or buying property of any kind
  - Leasing of property of any kind
  - Availing or rendering of services
  - Appointment of any agent for purchase or sale of goods, materials, services or property
  - Underwriting the subscription of any securities
Related Party Transactions – Some teasers

- Company intends to pay royalty to the holding company?
- Director wants to rent out his property to the company?
- A Company Secretary’s relative is proposed to be appointed as a Manager Finance?
- CEO wants to buy the car which has been allotted to him by the company?
- Can a company get a consolidated approval for multiple contracts?
When do I need to go to shareholders?

- For each transaction, if paid up capital of the company exceeds one crore, or,
- Transactions exceed 5% of the annual turnover or 20% of net worth, whichever is higher or,
- Appointment to office of profit at monthly remunerations exceeding one INR 1 lakh or,
- Underwriting fees exceeding INR 10 lakh

- Approval of central government not required
- Exemption in case of transactions in the ordinary course of business if done on an arms’ length basis
Interesting Concept of interested shareholder

- Member can not vote if it is a related party

Question

What will happen to contract between holding company and wholly owned subsidiary? Will there be a deadlock?

Way Forward for RPT

1. Define related party universe and possible transactions
2. Define mechanism to demonstrate Arms length basis
3. Obtain revised disclosures before start of FY 14-15
4. Prepare RPT guidance document for company and its employees
Loans to Directors

- Loans can only be given to WTD or MD:
  - As a part of employment terms applicable to all employees
  - Pursuant to a scheme approved by the special resolution

- Exemption to cases where loan is given in ordinary course of business at bank rate

- Interested person means:
  - Director of the holding co
  - any firm in Director or relative is a partner
  - a private company where such director is a director or member
  - Any body corporate whose Board / MD is accustomed to act in accordance with the instructions of its Board / Directors of lending company
Questions

1. Can section 186 / 372 A dilute the impact of section 185?

2. What about existing loans to subsidiaries and other companies?

3. Does interest need to be charged on existing loans?

4. Are Directors of subsidiary co accustomed to act in accordance with instruction of board of holding company? In all cases?
Key Messages

- Disclosure based regime
- Focus on governance
- Clear road map & action plan for compliance
**Corporate Social Responsibility (Schedule VII)**

1) Eradicating extreme hunger and poverty;
2) Promotion of education;
3) Promoting gender equality and empowering women;
4) Reducing child mortality and improving maternal health;
5) Combating human immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases;
6) Ensuring environmental sustainability;
7) Employment enhancing vocational skills;
8) Social business projects;
9) Contribution to the Prime Minister's National Relief Fund or any other Fund set up by the Central Government or the State Governments for Socio-economic development and relief and funds for the welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women; and
10) such other matters as may be prescribed.
**Clause 49 requirements**

### Board Disclosures – Risk management
The company shall lay down procedures to inform Board members about the risk assessment and minimization procedures. These procedures shall be periodically reviewed to ensure that executive management controls risk through means of a properly defined framework.

### Compliance
The Board shall periodically review compliance reports of all laws applicable to the company, prepared by the company as well as steps taken by the company to rectify instances of non-compliances.

### CEO/CFO certification
The CEO, i.e. the Managing Director or Manager appointed in terms of the Companies Act, 1956 and the CFO i.e. the whole-time Finance Director or any other person heading the finance function discharging that function shall certify to the Board that:

### Audit Committee - Related party transactions
A statement in summary form of transactions with related parties in the ordinary course of business shall be placed periodically before the audit committee.
**Internal Financial Controls**

“Internal Financial Controls” has been defined in the Act as to mean policies and procedures adopted by the company for ensuring:

- The orderly and efficient conduct of its business
- The safeguarding of assets
- The prevention and detection of frauds and errors
- The accuracy and completeness of the accounting records
- The timely preparation of reliable financial information

<table>
<thead>
<tr>
<th>Requirements and applicability (for various class of companies)</th>
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<tbody>
<tr>
<td>Requirement as per Companies Act 2013</td>
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<tr>
<td>Auditor’s report to comment upon adequacy of internal financial controls system (design as well as operating effectiveness)</td>
</tr>
<tr>
<td>Directors’ Responsibility Statement to state that directors, have laid down adequate internal financial controls and such controls are operating effectively.</td>
</tr>
<tr>
<td>The Independent Directors shall satisfy themselves on the integrity of financial information, and that financial controls and the systems of risk management are robust and defensible</td>
</tr>
<tr>
<td>Audit Committee’s terms of reference to include evaluation of internal financial controls and risk management systems</td>
</tr>
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**Monetary penalty up to Rs. 25 lacs**

**Imprisonment up to 3 years**

**Auditor’s qualification**

Companies Act 2013
**Woman Director – Some interesting Stats**

Analysis of a total of 404 companies which came out with IPO’s from 2002 and are listed on BSE

### Gender Categorisations of Board positions

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<tr>
<th>Gender</th>
<th>No of Directors</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Male</td>
<td>2,991</td>
<td>95%</td>
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<tr>
<td>Female</td>
<td>152</td>
<td>5%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>3,143</strong></td>
<td><strong>100%</strong></td>
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### Gender Frequency and Board representation

<table>
<thead>
<tr>
<th>Female Presence</th>
<th>No of Companies</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>No Female Director</td>
<td>277</td>
<td>69%</td>
</tr>
<tr>
<td>1 Female Director</td>
<td>103</td>
<td>25%</td>
</tr>
<tr>
<td>2 Female Directors</td>
<td>23</td>
<td>6%</td>
</tr>
<tr>
<td>3 Female Directors</td>
<td>1</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>404</strong></td>
<td><strong>100%</strong></td>
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