



# Compliance for Private Limited Companies

- G USHA, PRACTISING COMPANY SECRETARY

# Definition

- ▶ Restriction on transfer of shares
  - ▶ Limit on the number of members up to 200 (joint holders to be treated as single; further, present employee-members and past employees who became members during their employment and who continue to be members need not be counted for calculating the limit of 200)
  - ▶ Prohibition on invitation to the public to subscribe for any securities of the company.
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- ▶ Not a subsidiary of a public company.

# Articles of Association – Some clauses to pay attention to

- ▶ **Restriction** on transfer of shares – The nature and manner enforcement of the restriction need to be specified.
- ▶ General Meeting processes – can be customised to some extent in respect of sections 101 – 107 + 109
- ▶ Board Meeting processes – cannot be customised and the board processes as in SS-1 have to be followed.
- ▶ Director / MD/ WTD appointment processes to be well-defined as certain provisions of the Act are not applicable.
- ▶ First directors ideally to be mentioned in AoA. Otherwise subscribers to MoA will be deemed to be the first directors until they are duly appointed.
- ▶ Sec. 164/ 167 – additional conditions for disqualification and vacation may be included.
- ▶ Entrenchment provisions – useful for startups receiving VC funding, etc. for giving effect to veto rights of investors.

# Shares and Share Capital

- ▶ Section 43 – Kinds of share capital and Section 47 – Voting Rights are not applicable if the MoA or AoA so provides.
- ▶ Restriction on the right to transfer shares; the nature of the restriction or the procedure to be adopted must be clearly delineated to avoid disputes.
- ▶ Rights issue – concessions in timelines – if consent in writing of 90% of members of the company
- ▶ ESOP – Ordinary resolution for all private companies + exemption for start-ups - no prohibition for issue to promoter / promoter group / director holding more than 10% of outstanding equity shares (directly/indirectly, through relatives and any body corporate) - 10 years from incorporation.
- ▶ Sweat equity shares – normally – 15% of paid-up equity capital / issue value of Rs. 5 crores, whichever is higher; higher limit available for start-ups upto 50% of paid-up capital for 10 years from incorporation.
- ▶ Private placement - A company shall issue private placement offer cum application letter only after the relevant special resolution or Board resolution has been filed in the Registry: private companies shall file with the Registry copy of the Board resolution or special resolution with respect to approval under clause (c) of subsection (3) of section 179
- ▶ We need to keep in mind angel tax provision too!

# Issue of Debentures

- ▶ No restriction on the number of debenture holders (at least as far as NCDs go!)
- ▶ Beware of money raised being classified as a Deposit! If it's not any of the following, it's a deposit too!
  - ▶ Secured
  - ▶ Convertible
  - ▶ Listed
- ▶ Listing is possible, but the entity is not a listed company under the CA, 2013 but would be under the Listing Regulations.
- ▶ Valuation required or not?
- ▶ Canning Industries Cochin Limited vs SEBI – SAT order
  - ▶ OCDs – Sec. 62(3) – Treated as a separate species.
- ▶ Rights issue of debentures - possibility

# Deposits

- ▶ Loans or Deposits from Members
  - ▶ Are treated as deposits
  - ▶ Compliance requirements – Sec. 73(2)(a) to (f)
  - ▶ Exemption from the compliance requirements Sec. 73(2)(a) to (e) if:
    - ▶ Satisfying the 3-fold criteria – not an associate or subsidiary of any other company, borrowings from banks/FI or body corporate  $\leq$  Rs. 50 crores/2x capital, whichever is lower, no subsisting default in such borrowings
    - ▶ It is a start-up for 5 years from incorporation
    - ▶ Upto 100% of (PC+FR+SP)
    - ▶ Details of the above to be filed with the RoC in the manner as may be prescribed.
  - ▶ **However, once it is classified as a deposit, resolution needs to be passed and the Rules have to be adhered to.**
- ▶ Loan from promoters – Exempt only if conditions are met
- ▶ Loan from directors and directors' relatives – conditions to be met

# Borrowings and Advancing of Loans

- ▶ Section 179(3) applies; hence, only at meetings of the Board; but, Form MGT-14 need not be filed.
- ▶ Section 180 not to apply – So SR may not be needed; but AoA has to be adhered to.
- ▶ Section 185 applies to private companies that don't satisfy the 3-fold criteria;
  - ▶ no body corporate is a member,
  - ▶ borrowings from banks/FI or body corporate  $\leq$  Rs. 50 crores/2x capital, whichever is lower,
  - ▶ no subsisting default in such borrowings
- ▶ Section 186 applies to a private company.

# Board Processes

- ▶ At least 4 meetings in a year with a maximum gap of 120 days.
- ▶ Notice, agenda and agenda notes – minimum 7 days in advance.
- ▶ Shorter Notice:
  - ▶ Presence of one ID
  - ▶ If not, minutes to all; ratified by one ID
  - ▶ If no ID, majority of directors of Co.
- ▶ Notice cannot be sent by ordinary post. Hand delivery allowed.
- ▶ Proof of sending to be maintained for at least 3 years from the meeting.
- ▶ Applicable to any company which has borrowed money from banks and public financial institutions in excess of fifty crore rupees.



# RPT Compliance and Disclosure of Interest

- ▶ Exemption from Section 2(76)(viii) – Parties not considered as related parties for private companies!
- ▶ Audit committee requirements are not applicable – so all transactions with related parties are not covered under the compliance requirements; only related party transactions are covered.
- ▶ Section 188 compliance is required; however, relaxation is available for private companies from the restriction on voting rights of members who are related parties in respect of the transaction.
- ▶ Section 184:
  - ▶ Exemption only from participation in interested matters and not from disclosure per se!
  - ▶ Disclosure must be noted in the minutes
- ▶ Contracts / arrangements in respect of which compliance is required under section 148(2) is vague and the intent of law does not seem to be carried out under the provision.

# Appointment of MD / WTD

- ▶ Qualification Criteria
  - ▶ Age criteria
  - ▶ Solvency criteria
  - ▶ Conviction in respect of offences
  - ▶ Residency criteria
- ▶ Term of Appointment – 5 years at a time
- ▶ Restrictions on Appointment – A person can be the MD of maximum two companies. Unanimous approval of the Board and specific notice is required.

# Managerial Remuneration and provisions relating to KMP

- ▶ Processes and limits to be well-defined internally
- ▶ Office or place of profit provisions need to be remembered in case of remuneration paid in any other capacity.
- ▶ Remuneration in the absence of or inadequacy of profits
- ▶ All provisions applicable to KMPs are applicable to private companies too who choose to appoint KMPs.
- ▶ Form DIR-12 needs to be filed.

# Relaxations in respect of transactions with wholly-owned subsidiaries

- ▶ EGM can be held even outside India in case of WOS of a company incorporated outside India.
- ▶ Loans from holding co. to WOS will not attract Sec. 185.
- ▶ Loans/guarantee/security/investments beyond the limit in section 186 is possible without passing a SR if it is from a holding co. to WOS.
- ▶ Shareholders' approval under section 188 is not needed for transactions between a holding company and a WOS.
- ▶ Rule under the Section says holding company's resolution will suffice.
- ▶ Audit committee approval not required for transactions between holding company and WOS.

# Exemptions available only if 3-fold criteria satisfied

- ▶ Section 185 – Loan to directors
  - ▶ no body corporate is a member,
  - ▶ borrowings from banks/FI or body corporate  $\leq$  Rs. 50 crores/2x capital, whichever is lower,
  - ▶ no subsisting default in such borrowings
- ▶ Deposits – Exemption from compliance requirements and limit on deposit from members
  - ▶ not an associate or subsidiary of any other company,
  - ▶ borrowings from banks/FI or body corporate  $\leq$  Rs. 50 crores/2x capital, whichever is lower,
  - ▶ no subsisting default in such borrowings
- ▶ Section 67 – Restriction on purchase of own shares by company
  - ▶ no body corporate is a member,
  - ▶ borrowings from banks/FI or body corporate  $\leq$  Rs. 50 crores/2x capital, whichever is lower,
  - ▶ no subsisting default in such borrowings
- ▶ Beware, for claiming any exemption under the notifications – No default in annual filing!

# Exemptions available only for small companies

- ▶ Cash flow statement need not be prepared.
- ▶ Two board meetings in a calendar year with a minimum gap of 90 days (available for OPCs, startups and small companies)
- ▶ While counting the 20 companies an auditor is eligible to hold position in at a time: OPCs, dormant companies, small companies and private companies having paid-up capital less than Rs. 100 crores are exempt.
- ▶ Reporting on Internal Financial Controls with respect to Financial Statements and the operating effectiveness of such controls – not applicable to OPC, small co., private company having turnover less than Rs. 50 crores or aggregate borrowing from banks/FIs/bodies corporate **at any point in FY <= Rs. 25 crores.**
- ▶ Signing of Annual Return by CS/PCS is not needed (can't do too with the introduction of Form MGT-7A) (for OPC, small companies and start-ups)

# CARO Applicability

CARO is not applicable to:

- ▶ OPCs
- ▶ Small companies
- ▶ A private limited company:
  1. not being a subsidiary or holding company of a public company;
  2. having a paid-up capital and reserves and surplus not more than 1 crore rupees as on the balance sheet date; and
  3. not having total borrowings exceeding 1 crore rupees from any bank or financial institution at any point of time during the financial year; and
  4. not having a total revenue as disclosed in Scheduled III to the Companies Act (including revenue from discontinuing operations) exceeding 10 crore rupees during the financial year as per the financial statements.

# List of Compliance Requirements based on Thresholds

## ▶ On the basis of Paid-up Capital:

- ▶ Rs. 5 crore or more – XBRL filing
- ▶ Rs. 10 crore or more
  - ▶ Form MGT-8 certification and
  - ▶ Appointment of CS
- ▶ Rs. 50 crore or more – Rotation of Auditor
- ▶ Rs. 100 crore or more – Company included in limit of 20 companies for an auditor

## ▶ On the basis of Turnover:

- ▶ Rs. 50 crore or more – Annual Return certification
- ▶ Rs. 100 crore or more – XBRL
- ▶ Rs. 200 crore or more – Internal audit
- ▶ Rs. 1,000 crore or more – CSR



# List of Compliance Requirements based on Thresholds

## ▶ **On the basis of loans and borrowings from banks and FIs:**

- ▶ Rs. 50 crores or more
  - ▶ Rotation of auditor,
  - ▶ Vigil mechanism
- ▶ Rs. 100 crores or more
  - ▶ Secretarial audit,
  - ▶ Internal audit

## ▶ **On the basis of net worth:**

- ▶ Rs. 250 crore or more: Ind-AS
- ▶ Rs. 500 crore or more: CSR



Thank You, All!  
Happy Compliance!

- CS G Usha
- Practising Company Secretary