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Companies (Amendment) Act, 2020 – 10 key takeaways

Companies Amendment Act, 2020 (**Amendment Act**) amends the Companies Act, 2013 (**Principal Act**) and is the latest in a long line of amendments made since passing of Principal Act. Amendment Act, in its Bill form, had been passed by Lok Sabha on September 19, 2020 and by Rajya Sabha on September 22, 2020. It received the assent of the President on September 28, 2020 and became operative from that day onwards.

The amendments most likely to have a significant impact on India Inc are discussed here in below:

- **Reduction in penalties and decriminalization of certain offences not involving fraud:** Following in the steps of Companies (Amendment) Act, 2019, the Amendment Act also attempts to omit imprisonment as a punishment for a multitude of offences which are procedural and technical in nature. The amount of penalty too has been drastically reduced in many instances. Here are a few specific examples:
  - Where the contravention of provisions relating to issue of prospectus would attract a term of up to three years under the Principal Act, now the same has been completely done away with but the penalty amount has been maintained at the same level.
  - Regarding provisions relating to the requirement that investments made by a company are to be held in its own name, imprisonment has been removed, penalty has been reduced from INR 25,00,000 to INR 5,00,000 in case of a company and from INR 1,00,000 to INR 50,000 in case of officer in default.
  - Where a register of members is not maintained as provided for in the Principal Act, the punishment of continuing penalty has been replaced by introducing only a fixed amount of penalty.
  - The provision under the Principal Act of one person companies and small companies being liable only for 50% of the penalty mentioned in case of certain offences has been extended to all producer companies and start-up companies by the Amendment Act, subject to a maximum limit of INR 2,00,000 in case of a company and INR 1,00,000 in case of defaulting officer.
- **Exclusion of certain companies from the definition of ‘listed company’:** The Principal Act defines a ‘listed company’ as a company having any of its securities listed on any recognized stock exchange. Further, a reading of the private placement provisions under the Principal Act along with the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 permits certain private companies to list debt securities on a recognized stock exchange. These private companies are considered to be ‘listed companies’. Consequently, they become subject to strict compliance requirements (such as those relating to filing of annual returns, maintenance of records, appointment of independent directors & woman director, etc.) which are burdensome for such private companies to adhere to. Hence, the management of such companies tends to feel dis-incentivized from carrying out listing of the companies’ debt securities. The Amendment Act now empowers Central Government to exclude, in consultation with Securities and Exchange Board of India (**SEBI**), companies issuing specified classes of securities from the definition of ‘listed company’. While the relevant details will be prescribed in the rules after detailed consultations between Ministry of Corporate Affairs (**MCA**), SEBI and other stakeholders, hopefully with this amendment, private companies will no longer feel dis-incentivized to seek listing of their debt securities.
- **Reduction in timeline for applying for right issue:** A right issue is an offer made available for a specified period to existing shareholders of a company, which allows them to purchase further share capital in the company in proportion to their current holding. As per the Principal Act, a minimum time of 15 days is required to be given to the existing shareholders for them to accept the offer. Now, as per the Amendment Act, companies offering right issue will not be required to give a notice period of minimum fifteen days. This will help companies to raise funds in a quicker manner. While a 2015 notification of the MCA had previously provided a similar relaxation, this had been limited to private companies.
- **Direct listing option in foreign jurisdictions:** The Amendment Act empowers the Central Government to allow certain classes of public companies to list classes of their securities in permissible foreign jurisdictions. This amendment aims to allow for raising of funds from foreign markets to companies beyond listed companies, as was the case previously, and by easing current cumbersome regulatory requirements.
- **Declaration of Beneficial Ownership:** As per the previous norms under the Act, persons holding beneficial interest in the shares of a company are required to submit declarations to this effect and the company is required to file returns with the Registrar intimating such beneficial ownership. The Amendment empowers the Central Government to exempt, unconditionally or subject to conditions, certain classes of person(s) from the aforesaid requirements if it is considered necessary to grant such exemption in the public interest.

- **Periodic financial results:** Section 129A of the Amendment empowers the Central Government to require a certain class of unlisted public companies (which is yet to be prescribed) to prepare periodic financial results. Such periodic financial results are in addition to preparation of annual financial results prescribed under the Act and would need to be approved by the Board of Directors and audited (or subjected to a limited review) by the statutory auditors, in addition to filing periodic financial results with the Registrar. This requirement appears to have been introduced in alignment with similar provisions prescribed for listed companies under the LODR. Given that certain class of public companies will be permitted to list their securities in foreign jurisdictions, without listing on Indian stock exchanges, it is no surprise that the Amendment imposes an additional requirement on unlisted public companies to prepare periodic financial results thereby allowing the Central Government or the Ministry of Corporate Affairs (**MCA**) to keep a close watch on the functioning of such companies on a periodic basis and not just on an annual basis as per existing provisions of the Act.
- **Remuneration to independent directors:** The Principal Act specially provides for payment of remuneration to executive directors of a company, if in the year, the company has no profits or inadequate profits. The Amendment Act extends this provision to non-executive directors, including independent directors. This has been done in order to bring about alignment and to ensure retention of directorial talent in the company.
- **Significant changes in certain provisions relating to Corporate Social Responsibility (CSR):** Under the Principal Act, companies with net worth, turnover or profits above a specified amount are required to constitute a CSR Committee and spend at least 2% of their average net profits in the last three financial years towards CSR. The following amendments relating to CSR find their place in the Amendment Act:
  - Companies which have CSR spending obligation not exceeding INR 50,00,000 are now not required to constitute a Corporate Social Responsibility Committee
  - Where companies end up spending in excess of their CSR obligation in a particular financial year, the set of off of such excess spending will now be allowed to be made in subsequent years
- **Exemption to NBFCs:** Under the Act, a banking company is exempted from filing the resolutions passed to grant loans or give guarantee or provide security in respect of loans in the ordinary course of its business, with the Registrar. The Amendment extends such exemption to a registered non-banking finance company and a housing finance company.
- **Reduced timeframe for rectification of name and powers granted to the Central Government thereunder:** Prior to the Amendment, if the Central Government is of the opinion, on an application made to it by a registered proprietor of a trademark, that the name of a company is identical with or too closely resembles an existing trade mark, the company is required to change its name within a period of 6 months from date of directions issued by the Central Government in this regard. The Amendment now reduces this timeframe to 3 months. Additionally, Central Government is now empowered to allot a new name to the company (manner to be prescribed) if the company defaults in complying with directions issued by it and the Registrar is entitled to enter such new name in the Register of Companies in place of the old name and issue a fresh Certificate of Incorporation with the new name, which the company must use thereafter. However, none of the above changes restrict a company from subsequently changing its name, in accordance with the provisions laid down in the Act.

The Amendment Act has squarely addressed a range of issues that corporate India had been grappling with for some time now. It is, however, important to note that many of the amendments still require further clarification and the Amendment Act, 2020 with respect to overseas listing, scope of listed companies, beneficial ownership and other aspects will be tested once the Central Government notifies and prescribes corresponding rules in this regard. Needless to state, de-criminalization of menial offences revolving around procedural requirements and having no negative impact on the public interest will definitely go a long way on easing the burden on corporates from being criminalized for offences that are a product of inadvertent lapses and minor non-compliances with no intent to defraud the authorities or the public at large. All in all, this is a welcome move towards India’s goal to improve the ease of doing business in the country.

Third Amendment to Listing Regulations

The Securities Exchange Board of India (**SEBI**) has, on October 08, 2020, issued the SEBI (Listing Obligations and Disclosure Requirements) (Third Amendment) Regulations, 2020 (**Amendment**) amending provisions of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (**Listing Regulations**) in relation to disclosure requirements for listed entities and obligations with respect to listed debt securities. Below are the key changes proposed by the Amendment:

- **Asset cover:** Prior to the Amendment, entities that had listed their non-convertible debt securities (**NCDs**) were required to maintain an asset cover of 100% at all times. Further, the Listing Regulations also exempted regulated financial sector entities that issued unsecured debt securities for meeting capital requirements as specified by their respective regulators, from maintaining the aforesaid asset cover. However, the Amendment has done away with such exemption granted to regulated financial entities and now requires all entities (including regulated financial sector entities) with listed NCDs to maintain an asset cover of 100% or asset cover as per the terms of the offer document/Information Memorandum and/or Debenture Trust Deed, sufficient to discharge the principal amount at all times for such listed NCDs.
- **Intimation to debenture trustees:** Pursuant to the Listing Regulations, listed entities (which have their NCDs listed) are obligated to intimate debenture trustees regarding any revision in the rating, default in interest payments/redemption of NCDs or any failure to create charge on the assets. The Amendment introduces an additional obligation on listed entities to intimate their debenture trustees with respect to all covenants of the issue, including side letters, accelerated payment clauses, etc.
- **Half-yearly certificate:** Under the Listing Regulations, listed entities were required to mandatorily submit a half-yearly certificate regarding maintenance of 100% asset cover in respect of listed NCDs. In line with the permission granted by SEBI to maintain asset cover as per the terms of the offer document/Information Memorandum and/or Debenture Trust Deed, the half-yearly certificate shall now accordingly reflect compliance with the asset cover. Further, listed entities were earlier allowed to obtain this half yearly certificate from either a practicing company secretary or a practicing-chartered accountant, which is now required to be obtained from the statutory auditor of the listed entity. Additionally, the Listing Regulations exempted banks and non-banking financial companies registered with the RBI and bonds that are secured by a Government guarantee from submitting the half-yearly certificate to their debenture trustees. The Amendment now removes the exemption granted to banks and non-banking financial companies registered with the RBI, who will now be required to submit half-yearly certificates to their debenture trustees.
- **Disclosure of forensic audit:** Prior to the Amendment, there was no requirement for listed entities for disclosing details of the forensic audit to the stock exchanges/investors, except if considered material by the listed entity under Part B of Schedule III of the Listing Regulations. Addressing the gaps in the availability of information with respect to forensic audits of listed entities, the Amendment now requires all listed entities to disclose to the stock exchanges, without application of materiality, the fact of initiation of forensic audit along-with name of the entity initiating the audit and reasons for the same, if available, and a copy of the final forensic audit report received by the listed entity (other than those initiated by regulatory or enforcement agencies) with comments from the management, if any.

The Amendment focuses on bestowing debenture trustees with additional responsibilities and strengthening their role to protect the interest of debenture holders. Further, the requirement to disclose forensic audit of listed entities, without applicability of materiality, intends to bring about transparency for investors especially the public at large holding interests in listed entities to have adequate information about lapses in the entities, if any, which was otherwise not being disclosed or available in the public domain.

FCRA Amendment

The Ministry of Home Affairs, Government of India (**Government**) notified the Foreign Contribution (Regulation) Amendment Act, 2020 (**Amendment**) on September 29, 2020, in order to amend the extant provisions of the Foreign Contribution Regulation Act, 2010 (**Act**). The Act deals with acceptance and utilization of foreign contribution in the form of donation, transfer of any currency, security or article received from a foreign source by companies or associations (**Recipients**).

In the backdrop of the recent cancellation of more than 19,000 certificates of registration of recipients, this Amendment aims to streamline and strengthen the compliance mechanism in order to bring about greater transparency and accountability with respect to acceptance and utilization of foreign contribution. Some of the key changes introduced by the Amendment are discussed below:

- **Embargo on 'public servant' as Recipient:** The Act essentially prohibits certain persons from receiving foreign contribution. The list under Section 3 of the Act includes judges, members of any legislature, government servant, political party, etc. The list is now revised to include 'public servant' as defined in Section 21 of Indian Penal Code, 1860, in order to help curb the potential exploitation of the functions entrusted upon public servants.
- **Complete ban on transfer of foreign contribution:** Prior to the Amendment, Recipients were permitted to transfer foreign contributions to others registered under the Act read with the Rules framed thereunder. The Amendment has now been put a complete ban on such transfers by significantly altering the position under Section 7 of Act and prohibiting such persons authorized under the Act to accept foreign contributions from transferring such foreign contributions to any other person. While such prohibition might pose certain challenges for companies seeking foreign contributions, this is a positive step from a governance and financial accountability perspective.
- **Government empowered to prohibit a recipient from utilizing/receiving its funds:** Pursuant to addition of a proviso to Section 11 of Act, the Government is now empowered to prohibit a Recipient from utilizing or accepting foreign contribution. As per the Amendment, this shall be resorted to only in the event that the Government, based on a summary inquiry, believes that such person has contravened provisions of the Act. As a result, treatment of unutilized foreign contribution of the Recipients can now be restricted by the Government upon any prima facie contravention under the Act.
- **Maximum time period for suspension of certificate of registration increased:** The provisions relating to Section 13 of Act allow the Government to suspend the certificate of registration of Recipients, following which the Recipients cannot accept or utilize the foreign contributions. Such suspension of certificate of registration of Recipients can be for a maximum period of 180 days. Pending any inquiry for cancellation of such registration, the Amendment extends this to a period up to 360 days.
- **Extent of administrative expense lowered:** As per the previously existing norms under the Act, the Recipients were permitted to deploy about 50% of foreign contribution to discharge administrative expenses, which has now been reduced to merely 20% by the Amendment. The Rules framed under the Act enumerate as to what constitutes as administrative expense such as payment of salaries, travel expenses, consumables like water/electricity, rent, operational costs, etc.
- **Bank account mandate in State Bank of India, Delhi:** The Recipients are required to open a designated account in any of the Scheduled Banks in order to receive foreign contributions. The Amendment mandates the Recipients to open a designated account in a branch of State Bank of India at New Delhi, through which the Recipients will now receive foreign contributions. However, Recipients are also permitted to open accounts in other Scheduled Banks for the purpose of utilizing the foreign contribution. The intention behind such mandate is to monitor and centralize the inflow of foreign contributions.
- **Mandatory identification requirements:** The Amendment now enables the Government to require Aadhaar Card as identification document during application for approval or for certificate of registration (or renewal thereof) of the potential Recipients. All the office-bearers or the key functionaries of the potential Recipients are mandatorily required to provide their Aadhaar numbers for said purposes. In case of foreigners, he/she is required to submit a copy of passport or Overseas Citizen of India card as an identification document.

Conclusion

There has been a crucial increase in the inflow of foreign contribution in past few years and the Government has brought about this Amendment to obstruct malicious funding from foreign sources. However, the Amendment seems to have skewed the balance between ensuring compliance and operational flexibility for businesses. The stated objectives of Government for this Amendment – to 'strengthen compliance mechanism, enhance accountability and facilitation in receiving foreign contribution' – have been stretched too far, leading to onerous and cumbersome requirements placed upon the Recipients while simultaneously strengthening the Government's authority to intervene.

RBI issues FAQs on one-time loan restructuring scheme for Covid-19 related stress

Reserve Bank of India (**RBI**) has allowed one-time restructuring of loans without directly classifying them as Non-Performing Asset (**NPAs**) to assist the companies and individuals to revive and manage the financial stress that is caused by the Covid-19 pandemic.

According to RBI, the lenders must ensure that the restructuring scheme that was announced on August 06, 2020 (**Resolution Framework**) is only available to borrowers that are facing stress due to the Covid-19 pandemic. The Resolution Framework is not available for exposure to financial sector entities as well as Central and State governments, local government bodies and anybody corporate that is established by an act of parliament or state legislature.

In this context, RBI has released frequently asked questions (**FAQs**) on the Resolution Framework on October 13, 2020. With these FAQs, RBI has addressed number of queries on operational issues. Some of the pertinent aspects of the FAQs have been set out below:

- The Resolution Framework allows banks to restructure the loans of eligible borrowers (i.e. individuals and entities classified as standard) that were regular in their repayments and did not default for more than 30 days as of March 01, 2020, without downgrading their asset classification. The timelines within which the resolution plan can be invoked and implemented is provided. Only the resolution plans invoked before December 31, 2020 will be considered. Meaning of the terms 'invocation' and 'implementation' has been defined in the FAQ.
- The farm credit exposure of all lending institutions, including NBFCs, is excluded from the scope of the Resolution Framework. However, loans to farm related activities such as dairy, poultry, fishery, animal husbandry, bee-keeping and sericulture would be eligible for the resolution scheme if they fall within the purview of 'personal loans'. The loans given to farmer households would be eligible for resolution if they do not meet any other conditions for exclusions listed in the Resolution Framework.
- There are loans that are granted to individuals where the property is in the name of the individual, but a related company/non-individual entity is a co-borrower in the loan structure to augment the income for repayment. Such advances would not be treated as personal loans as per circular DBR.No.BP.BC.99/08.13.100/2017-18 dated January 04, 2018. However, they would have to be dealt under a scheme for resolution of other exposures.
- The requirement of inter-creditor agreement is mandatory for implementation of resolution plan as well as for real estate sector; however, the prescribed thresholds for financial parameters that are issued under RBI circular dated September 07, 2020 may be applied for real estate sector at the project level. Further, restructuring in respect of projects under implementation involving deferment of Date of Commencement of commercial operations is excluded from scope of Resolution Framework.
- Resolution Framework is applicable to all eligible borrowers, subject to the exclusions that have been prescribed in paragraph 2 of Annex to the Circular on Resolution Framework dated 07 September 2020 (**Circular**). In respect of those sectors where the sector-specific thresholds have not been specified in the Circular, lending institutions shall make their own internal assessments.
- Financial parameters issued under the Circular are applicable to all borrowers in respect of whom the resolution has been undertaken in terms of Part B of the Annex to the Circular.
- Only the resolution plans that receive a credit opinion of RP4 or better for the residual debt from a Credit Rating Agency shall be considered for implementation under the Resolution Framework. In case credit opinion is obtained from more than one CRA, all such credit opinions must be RP4 or better. This clarity will aid many small and medium businesses to become eligible for corporate loan restructuring/recasting.
- The new definition of micro, small and medium enterprises effective from July 01, 2020, will not impact their eligibility for resolution but will be based on the definition that existed as of March 01, 2020.

Regulatory changes in the AIF regime in India

Investments in Alternative Investment Funds (**AIFs**) in India are governed by the securities market regulator, Securities and Exchange Board of India (**SEBI**). In 2012, SEBI had issued the SEBI (AIF) Regulations, 2012 (**Regulations**) to regulate the formation and investments by AIFs. Recently, SEBI has notified 3 key changes to the management framework of AIFs vide its notification dated October 19, 2020[1] (**Notification**) and circular dated October 22, 2020[2] (**Circular**). The changes primarily deal with enhanced eligibility criteria for investment team of AIF, imposing responsibility on the investment committee and clarification on membership of non-resident Indian citizens in investment committees.

Key takeaways

- **Enhanced qualification criteria for the key investment team:** The Notification has enhanced the qualification criteria for the key investment team, requiring the team to have adequate experience, with the following specifications:
  - At least 1 key personnel with minimum 5 years of experience in advising or managing pools of capital/ fund etc.
  - At least 1 key personnel with professional qualification in finance, accountancy, business management, commerce, economics, capital market or banking from a University or an institution recognized by the Central Government or any State Government or a foreign university, or a CFA charter from the CFA institute or any other qualification as may be specified by SEBI

  The Notification aims to specify the scope of qualifications required by the investment team in AIF, which was earlier cryptic in its description. This will seek to ensure that the investment team consists professionals having adequate qualification and experience to understand the investment decisions of AIF and protect the interests of investors.
- **Regulating the constitution of investment committee:** The second change introduced by SEBI is by regulating the constitution of investment committee by investment managers. Until now, while it is common for AIFs to constitute an investment committee to vet and approve investment decisions made by the investment manager, the Regulations did not regulate the functioning of such investment committee. The Notification amended Regulation 6 of the Regulations to also provide for the following conditions:
  - That the members of investment committee shall be equally responsible as the investment manager for investment decisions of AIF
  - That the investment manager and members of investment committee shall ensure that AIF investments are in compliance with Regulations, the placement memorandum, agreement with investor, any other fund documents and any other applicable law
  - External members whose names are not disclosed in the placement memorandum or agreement with investor or any other fund documents at the time of on-boarding investors, shall be appointed to the investment committee only with the consent of at least 75% percent of the investors by value of their investment in AIF or scheme
- **Membership of non-resident Indian citizens in investment committees:** Vide the Circular, a clarification has been issued by SEBI on membership of non-resident Indian citizens in investment committees as external members. The investment committees proposed by investment managers would consist of internal members (employees, directors/ partners of the investment manager) and/or external members., which could include non-resident Indian citizens as external members. As a result, SEBI had sought clarification from the Central Government and the Reserve Bank of India on the applicability of Schedule VIII (4) of the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 (**Non-Debt Rules**) to the investments made by AIF whose investment committee consists of non-resident Indian citizens as external members. As per Schedule VIII (4) of the Non-Debt Rules, downstream investment by an AIF shall be considered foreign investment if the sponsor or investment manager is owned and controlled by persons resident outside India. However, a clarification is yet to be received by SEBI from Central Government and RBI. Pending such clarification, SEBI has clarified as follows:
  - Applications by AIFs under which investment committees are proposed to be formed with external members who are resident Indian citizens would be duly processed by SEBI
  - Applications under which investment committees are proposed to be formed with external members who are non-resident Indian citizens, will be processed by SEBI only after a clarification is received from Central Government and RBI

Key takeaways

By way of the Notification and Circular, SEBI has brought much needed and awaited guidelines on the requirement of professional qualification for the team of investment manager and the same will seek to add a professional layer to the management of AIFs. The involvement of an investment committee in fund management was already a standard practice for better management of the fund. However, the regulation of such committees is definitely a welcome move and will increase transparency and accountability, particularly in terms of fund management philosophy. Lastly, the clarification sought by SEBI from Central Government and RBI will be a determinant factor on participation of non-resident Indian citizens in the investment committees of AIFs.

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[1] Notification No. SEBI/LAD-NRO/GN/2020/37
[2] Circular No. SEBI/HO/IMD/DF6/CIR/P/2020/209

Scheme for grant of ex-gratia payment of difference between compound interest and simple

Ministry of Finance, Government of India, on account of unprecedented situation arising because of Covid-19, vide notification dated October 23, 2020 has approved a scheme for the grant of ex-gratia payment of difference between compound interest and simple interest for six months to the borrowers of specified loan accounts (**Scheme**).

The key terms of the guidelines of the Scheme are provided below:

- **Eligibility of borrowers:** Borrowers who have availed MSME loans, education loans, housing loans, consumer durable loans, credit card dues, automobile loans, personal loans, consumption loans are eligible to avail benefits under this Scheme. Provided that the sanctioned limit and outstanding amount does not exceed Rs. 2,00,00,000 (aggregate of all facilities with lending institutions) as on 29 February 2020. The benefits under the Scheme are subject to the following conditions and stipulations:
  - Account should be standard as on February 29, 2020, i.e., loan should not be a non-performing asset as on February 29, 2020.
  - Lending institution must be either a banking company, or a public sector bank, or a co-operative bank, or a regional rural bank, or an All India Financial Institution, or a Non-Banking Financial Company or a Housing Finance Company registered with RBI or National Housing Bank as the case may be. A Non-Banking Financial Company - Micro Finance Institution should be a member of a Self-Regulatory Organization recognized by RBI.
  - The ex-gratia payment under the Scheme shall be admissible irrespective of whether the borrower had fully availed or partially availed or not availed of the moratorium on repayment announced by RBI ride its circular DOR. No. BP.BC.47/21.04.048/ 2019-20, dated 27 March 2020 and extended on May 23, 2020.
- **Other terms and conditions**
  - The period to be reckoned for crediting of difference between the compound interest and simple interest under the Scheme would be from 01 March 2020 to 31 August 2020 (184 Days/6 months). For the accounts closed during said period, the period of crediting would be from 01 March 2020 to the date of closure of such account.
  - The benchmarks and modalities for ex-gratia payment of difference between compound interest and simple interest under the Scheme would be as detailed in the operational guidelines.
  - The rate of interest would be as prevailing on February 29, 2020, i.e. in case the rate of interest has changed thereafter, it shall not be reckoned for the purposes of this computation. The subject amount shall be credited to the account of the borrower by the respective lending institutions as ex-gratia payment under the Scheme.
  - The aforesaid exercise of crediting the amount in the accounts of the eligible borrowers by their respective lending institutions shall be completed on or before November 05, 2020.
  - Lending institutions can lodge their claim for reimbursement latest by December 15, 2020. Claims shall be submitted to the designated officer/cell at the State Bank of India (**SBI**).
  - Each lending institutions shall put in place a grievance redressal mechanism for the eligible borrowers for redressal of their grievances arising out of the Scheme within one week from the date of issuance of the Scheme at appropriate levels.

    Grievances, if any, of the lending institutions shall be resolved through the designated cell at SBI in consultation with the Ministry of Finance, Government of India.

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