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STANDING COMMITTEE ON FINANCE
(2011-12)

FIFTEENTH LOK SABHA

MINISTRY OF CORPPORATE AFFAIRS

THE COMPANIES BILL, 2011
FIFTY SEVENTH REPORTS

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LOK SABHA SECRETARIAT
NEW DELHI

FIFTY SEVENTH REPORT
STANDING COMMITTEE ON FINANCE

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PART – I

I. INTRODUCTION

1.1 The companies Act, 1956 had been enacted with the object to consolidate and amend the law relating to the companies and certain other Association. The said Act has been in force for about fifty five years and had been amended 25 times. The number of the companies has expanded from about 30000 in 1956 to nearly 8 lakhs companies functioning as of date. A number of changes have taken place during the last 2-3 decades in the national and international economic and regulatory environment. The Indian economy has also experienced substantial expansion and growth. The change in regulatory structure for corporate sector was also considered necessary to address issues relating to regulatory harmony, recognition of good corporate practices and technological improvements.

1.2 Keeping in view the above factors, the central government after due consultations and deliberations decided to repeal the Companies act, 1956 and enact a new legislation to provide for new provisions to meet the changed national and international economic environment and accelerate the expansion and growth of our economy.

1.3 A Concept paper on company Law was placed on the Ministry's official Web-site on August 4, 2004 for suggestions/comments by all interested stakeholders. A large number of comments, responses and suggestions were received. To examine these comments, responses and suggestions and to advice the central Government on various issues, the government constituted an expert Committee under the Chairmanship of Dr. J.J. Irani, director, Tata sons Ltd. This committee included representatives from various industry and trade bodies/ associations, statutory professional bodies, experts and Representatives from regulatory bodies such as reserve Bank of India (RBI), Securities and Exchange Board of India(SEBI) and concerned Ministries/ Departments.

1.4 The committee submitted its report to the government on 31st May, 2005. The Report of Dr. Irani committee, in addition to publication on the web site of the Ministry was also circulated to all Central Ministries/ Departments, chief Secretaries of state Governments and various chambers/ professionals Institutes. Taking into account the principles enunciated in the report of the Irani Committee and views, comments and suggestions

received by the Ministry from various quarters, the companies bill, 2008 was prepared.

1.5 The companies bill 2008 was introduced in the lok sabha, which was subsequently referred to the parliamentary Standing committee on Finance for examination and report. However, before the committee could present its report, 14th Lok Sabha was dissolved and the companies Bill, 2008 lapsed as per clause, (5) of article 107 of the constitution of India. In view of this, it was proposed to re-introduce the Companies Bill, 2008 as the companies bill ,2009 without any change except for the bill year and the Republic Year. The Companies Bill, 2009 accordingly, was introduced in the Lok Sabha on 3rd August, 2009.

1.6 After introduction, the companies bill, 2009 was referred to parliamentary Standing committee on finance for examination and report. the committee examined the same in detail in consultation with various stakeholders including the Administrative Ministry and submitted a comprehensive report to the Parliament on 31st august, 2010. Keeping in view the recommendation made by the Standing committee, a revised Companies Bill, 2011 was prepared which was approved by the cabinet on 24th November, 2011. This bill was introduced in the Lok Sabha on 14th December, 2011. The Hon'ble Speaker referred the bill to parliamentary Standing Committee on finance on 5th January, 2012 as certain new provisions were included in the Bill, which were not earlier referred to the Committee during the examination of companies Bill,2009.

1.7 According to the Ministry of Corporate Affairs, most of the recommendations made by the Committee in their earlier Report(21st Report) on the Companies Bill, 2009 have been accepted by the government and Incorporated in the Companies Bill, 2011. In a statement furnished to the Committee, they have submitted that out of 178 recommendations made by the Committee, 167 have been incorporated fully, Six have been partially incorporated and in respect of five recommendations, a different have been taken as indicated in the statement given below:-

II. New Provisions introduced in companies Bill, 2011-

2.1 while Incorporating the Several recommendation of the committee, as also some of the suggestions/ representations received subsequent to submission of report of committee, the provisions of the Companies bill,

2009 were revised and the fresh bill was formulated as companies Bill, 2011 and introduced in parliament. A statement indicating the changes made and the new provisions introduced has been submitted by the Ministry..

Salient Features of the Companies Bill, 2011.

3.1 The following are the salient features of the Companies Bill, 2011:-

(i) E-Governance :- Maintenance and allowing inspection of documents by companies in Electronic from being allowed for the first time.

(ii) Concept of Corporate Social Responsibility is being Introduced.

(iii) Enhanced Accountability on the part of Companies:

(a) In addition to the concept of Independent directors (IDs) introduced, the provisions in respect of their tenure and liability, etc. have been provided. Code for IDs provided in a new Schedule to the Bill. Databank for IDs proposed to be maintained by a body/ institute notified by the Central government to facilitate appointment of IDs.

(b) Corporate Social Responsibility (CSR) Committee of the Board proposed in addition to other committees of the Board Viz Audit Committee, Nomination and remuneration and Stakeholders Relationship committee. These Committee shall have IDs/non executive directors to bring more independence in Board functioning and for protection of interest of minority shareholders.

(c) Definition of “Promoter” also included along with his liability in certain cases.

(d) Provision in respect of vigil mechanism (Whistle blowing) proposed to enable a company to evolve a process to encourage ethical corporate behaviour, while rewarding employees for their integrity and for providing valuable information to the management on deviant practices.

(e) The Central Government has been empowered to prescribe restriction in respect of layers of subsidiaries for any class or classes of companies.

(f) New provisions suggested for allowing re-opening of accounts in certain cases with due safeguards.

(iv) Additional Disclosure Norms:-

(a) New Disclosure like development and implementation of risk management policy, Corporate social Responsibility Policy, manner of formal evaluation of performance of Board of directors and Individual directors included in the Board report in addition to disclosures proposed in such report in the Companies Bill, 2009.
(b) Consolidation of Accounts: Accounts of Foreign Subsidiaries to be attached for filing them with the Registrar. Subsidiary to include "associate" and "Joint venture" for the purpose of consolidation.
(c) Every listed company required to file a return with the registrar regarding change in the shareholding position of promoters and top ten shareholders of such company.

(v) Facilitating raising of capital by companies:

(a) Provisions for offer or invitation for subscription of securities on private placement basis revised to ensure more transparency and accountability.

(b) Companies being allowed to issues equity shares with differential voting rights.

(c) Central Government empowered to prescribe, through rules, the requirements in connection with provision for money made by a company for allowing purchase of company's shares by its employees under a scheme for their benefit. Disclosure to be made in the Board's report in respect of voting rights not exercised directly by the employees in respect of voting rights not exercised directly by the employees in respect of shares to which the schemes relates.

(vi) Audit Accountability:

(a) Rotation of auditors and audit firms being provided for.
(b) Stricter and more accountable role for auditor being retained. Provisions relating to prohibiting auditor from performing non-audit services revised to ensure independence and accountability auditor.

PART-II

OBSERVATIONS / RECOMMENDATIONS

1. The Committee had examined the Companies Bill, 2009 at length and presented a comprehensive Report to Parliament on 31 August, 2010 after a great deal of deliberation, considering carefully the suggestions / views submitted by different stakeholders and holding extensive discussions with the Ministry of Corporate Affairs, SEBI, RBI, Industry / Trade Associations, Professional bodies like Institute of Chartered Accountants of India, Institute of Company Secretaries of India and Institute of Cost Accountants of India. The Committee also heard the views of some experts on the subject. 2. The Committee note with satisfaction that the Companies Bill, 2011, although introduced by Government as a fresh Bill (in view of several amendments required), contains salutary provisions which seek to usher in a contemporaneous corporate law in the country, incorporating most of the recommendations made by the Committee in their Report.

3. However, as the Companies Bill, 2011 also included certain new provisions and suggestions, which were not earlier referred to and considered by the Committee, it was referred again to the Committee for examination and report. Accordingly, the Committee decided to invite suggestions from experts / stakeholders on these new proposals in the Bill. In response, the Committee received a large number of suggestions not only on the new proposals, but also on some general issues as well as points already covered and commented upon in their earlier Report. The Committee are happy to note that most of these suggestions, which are not contrary to the Committee's earlier recommendations, have since been accepted by the Ministry. The Committee would expect that these suggestions would be appropriately incorporated in the Bill and the concerned clauses modified accordingly. The Committee further note that the Ministry have not agreed to some of the suggestions and have expressed a contrary view thereon. The Committee would like to deliberate

and comment upon these suggestions as follows :- 4. On the suggestion that, the term „private placement" (clause 42) be defined, the Ministry have submitted that in view of the detailed treatment of all aspects of the subject and the fact that „public offer" has been defined (Explanation to Clause 23), there is no need to further define the term. The Committee would however strongly recommend that as the Bill seeks to regulate a new and widely adopted method of raising capital, it would be fair and useful that „private placement" is properly defined in the statute. The Committee also desire that the position of Bill as recommended by the Committee in their earlier Report presented to Parliament in August, 2010 needs to be maintained, to allow raising capital / borrowings by way of private placement by corporates / entities so that they can harness their capabilities and resources available with them.

5. The Committee note that Clause 61 requires the Company to obtain the approval of the Tribunal to consolidate/subdivide its share capital. Since consolidation or subdivision of shares does not affect the voting power of the shareholders, the Committee recommend that the said clause be modified to the extent that in cases of consolidation or sub-division of share capital, the approval of the Tribunal would be required only if the voting percentage of shareholder is changed. 6. The Committee desire that time lines may be prescribed in the conditions stipulated in regard to purchase of own shares by companies, namely, filing of annual returns / financial statements, timely distribution of dividend etc. in the interest of greater accountability. 7. It has been suggested that the provisions of existing Act where shareholders appoint auditors at every Annual General Meeting (AGM) be continued in the interest of accountability to shareholders. The Committee would recommend that the proposal in the Bill [Clause 139(1)] for appointment of auditors for straight five years may be modified to the extent that the process be subject to ratification at every AGM. The Committee believe that the well-established principle of

shareholders‟ democracy represented by the Annual General Meeting of the company should be preserved, while seeking to provide stability of tenure to auditors. 8. Similarly, the Committee desire that the suggestion to review the provision in Clause 139(3) allowing members of a company to pass a resolution requiring the partner in an audit firm to be rotated every year may be considered positively by the Ministry by substituting the words „every year„ with „at such interval as may be resolved by Members„. 9. With a view to achieving the objective of rotation of auditors, the Committee would like to further recommend that the proviso to Clause 141(3)(g) empowering members of a company to pass resolution to reduce number of companies in which auditor/ audit firm shall become auditor may be omitted. The Clause may thus clearly provide for the maximum number of companies a person can be appointed as auditor of, as provided for in the case of directors of companies. In this context, the Committee would also like to endorse the provision prescribing liabilities for auditors and extending them to the audit firm as well, since the distinction between the two is rather tenuous. The Committee are of the view that the safeguards provided in the Bill to ensure professionalisation and integrity of the audit process are necessary and optimal. 10. The Committee note that Clause 466 *inter-alia* allows Members of Company Law Board (CLB), who are eligible under the new Bill, to be appointed as Members of National Company Law Tribunal (NCLT). According to the Ministry, this provision is required to ensure continuity in functioning. The Committee apprehend that this should not result in defect conversion of existing CLB benches into NCLT benches. As during the course of examination of the Demands for Grants of the Ministry of Corporate Affairs, the Committee have found the working of the CLB Benches to be far from satisfactory, it would be prudent that the constitution / selection process for NCLT is initiated de novo.

11. It has been suggested that similar to Section 90 of existing Act, a savings provision may be introduced exempting a private company from

restrictions with regard to types of share capital / voting etc. to provide flexibility to such companies. According to the Ministry, such exemptions to class of companies can be given through notifications. The Committee would however re-iterate their earlier recommendation on this issue that the exemptions available for different classes of companies like private company, one person company etc. may be clarified, as far as possible, in the Bill itself. 12. The Committee note an important suggestion made by the C&AG of India to include in the Companies Bill disclosure provisions in the report of the Board of Directors [Clause 134(3)] indicating the impact / implications of Government directives on the financial position of a Government Company. Although, the Ministry of Corporate Affairs as well as the Department of Public Enterprises have not agreed with this suggestion, the Committee are of the view that the suggestion of the C&AG is worth considering in the interest of functional autonomy and operational efficiency of PSUs. It will also help minimize Government interference in the management of PSUs. 13. The Committee are of the view that corporates in general are expected to contribute to the welfare of the society in which they operate and wherefrom they draw their resources to generate profits. Accordingly, the Committee recommend that Clause 135(5) of the Bill mandating Corporate Social Responsibility (CSR) be modified by substituting the words „shall make every endeavour to ensure" with the words „shall ensure". Further, the Committee recommend that the said clause shall also provide that CSR activities of the companies are directed in and around the area they operate.

14. The Committee note that in clause 147(2) and clause 147(3), it is provided that if there is a non-compliance by the auditor of the specified provisions and the contravention is with an intent to deceive the company or its shareholders or creditors or any other person concerned or interested in the company, then he shall be liable to a prescribed fine. The Committee further note that the term "any other person concerned or

interested in the company" has potential for abuse. The Committee, therefore, are of the view that applying an open-ended test of liability without defined restrictions may result in undesirable situation of creating a liability which is not defined in terms of area, duration and amount and may expose the auditor to uninsurable risk. Accordingly, the Committee recommend that the clause 147(2) and clause 147(3) be suitably modified, clearly defining the term „or any other person concerned or interested in the company". Further, in order to provide for punishment under Clause 447 for fraud to those partners of audit firm who acted in a fraudulent manner, the Committee recommend that Clause 147(4) of the Bill be modified to the extent that „such partner or partners of the audit firm" be replaced by „such concerned partner or partners of the audit firm". 15. As regards the suggestion to exempt investments made in securities issued by the PSUs from the provisions of Clause 186 relating to Loan and Investments by companies, the Committee accept the Ministry's clarification that the bonds issued by any company including a government company, engaged in the business of financing of companies or of providing infrastructural facilities would be exempted from the requirements of Clause 186 by virtue of exemption sub-clause 186(11).

16. With regard to the suggestion that the rate of interest on inter-corporate loans should be linked to the yield on Government of India dated securities of equivalent maturity instead of the prevailing bank rate under the RBI Act, the Ministry have submitted that detailed consultations are required in this regard with Ministry of Finance and RBI. When the bank rate was prescribed as a benchmark for inter-corporate loans /investments, it was the major policy rate at that time and market related benchmarks had not stabilized yet. However, now that the dated government securities market is well developed with enough liquidity precluding any manipulation of yields, this may very well replace the bank rate as the benchmark. The Committee would like the Ministry to consider this suggestion in the

current economic perspective. 17. The Committee had recommended in their earlier Report that whole-time Director should be included within the definition of Key Managerial Personnel (KMP), even if the company has Managing Director / Manager. According to the Ministry, whole-time directors may not be brought within the purview of KMPs, as they do not exercise substantial powers of management where Managing Directors are in position. The Committee, while disagreeing with the Ministry's view in this case, would like to reiterate their earlier recommendation, as whole-time directors, being important functionaries in a company with substantial role in decision-making, cannot be kept outside the purview of KMPs.

18. The Committee in its 21st report on Companies Bill 2009 had emphasized that transgressions, purely procedural or technical in nature, should be viewed in a broader perspective, while serious non-compliance or violations including fraudulent conduct should invite stringent /deterrent provisions. However, the Committee observe that there are many instances in the Bill where criminal liability have been imposed for technical mistakes of law like Clause 157 (failure to file DIN with Registrar of Companies), Clause 56 (delay in registering transfer of shares within the prescribed period), Clause 117(2) (failure to file certain agreements and resolutions with Registrar of Companies), etc. The Committee reiterate the principle enunciated in its previous report that technical defaults which are minor infractions of law should not carry criminal liability. Accordingly, the Committee recommend that all such clauses in the Bill which impose criminal liability for technical defaults may be modified suitably. 19. Clause 2(52) of the Bill defines "Listed Company" as a company which has any of its securities listed on any recognized stock exchange. "Securities" would thus include all instruments including bonds, debentures etc. It has been suggested that with a view to accord some freedom and flexibility of operations to Companies, specially when public funds are not involved, the above definition may be amended to limit the applicability only to : (a) Companies where the equity shares or any security convertible into equity

shares are listed; or (b) companies where the debt instruments are listed, having been issued to public at large. The Committee find merit in the argument from operational perspective that the scope of above definition of "Listed Company" may be confined to listed securities issued through the process of „Public offer" [as defined in clause 23(1)] only, so that the regulatory framework can focus on such instruments only without dissipating energy and resources on all kinds of instruments, since the unlisted instruments are already subject to scrutiny of Ministry of Corporate Affairs. The Ministry of Corporate Affairs may accordingly consider appropriate modification in the definition of "Listed Company" in consultation with Ministry of Finance.