



# REGULATORY UPDATES

Proposals Under the Company Law Committee (2022)

## PROPOSALS UNDER THE COMPANY LAW COMMITTEE (2022)

The Company Law Committee presented its Report dated March 21, 2022 to Honourable Union Minister of Corporate Affairs on changes aimed at facilitating and promoting greater ease of doing business in India and effective implementation of the Companies Act, 2013, the Limited Liability Partnership Act, 2008 and the Rules made thereunder.

The Report recommends various changes to the Companies Act, 2013 to recognise new concepts, expedite corporate processes, improve compliance requirements, and remove ambiguities from existing provisions.

Certain key proposals suggested by the committee are as follows:

### 1. Introduction of Restricted Stock Units (RSUs) and Stock Appreciation Rights (SARs)

The Committee proposes to introduce new Schemes to compensate Employees, linked with Shares such as Restricted Stock Units (RSUs) and Stock Appreciation Rights (SARs). Presently, recognition to ESOPs and Sweat Equity Shares have been given under the Companies Act, 2013.

Under **RSUs** the employee will be entitled to the shares at the end of the vesting period, so long as the restrictions concerning the duration of employment and performance parameters are met. It does not give the employee an option to purchase or subscribe to the share directly, unlike ESOPs.

**SARs** are a form of deferred compensation tied to the employing company's stock performance. It gives employees the right to the monetary equivalent of the appreciation in the value of a specified number of shares over a specified period. The settlement of the SARs may also be made by way of shares of the Company.

## **2. Constitution of Risk Management Committee (RMC)**

To strengthen the Board's power to overview and supervise risk managements systems, it has been recommended to include provisions for constitution of Risk Management Committee (RMC) for certain classes of Companies.

Presently, there's a provision of setting up RMC and formulating the framework to identify and mitigate risks under SEBI regulations and there's no such provision under the Companies Act, 2013.

## **3. Strengthening of Audit Framework**

Suggestions have been made to Strengthen the Audit Framework given the importance of audits and the crucial role of Auditors in corporate governance.

### **a) Auditors to make detailed disclosures to stakeholders before resigning**

The Committee proposes to make changes in the provisions governing resignation of auditors and it suggests the requirement to make detailed disclosures before resignation. The auditors should specifically mention whether the resignation is due to non-cooperation from committee, fraud, severe non-compliance or diversion of funds.

### **b) Mandatory joint audit for certain Companies**

Currently, under the Companies Act, 2013, carrying out a joint audit is the prerogative of the company's members. The Committee proposes to make Joint Auditors mandatory in public interest for certain prescribed class of Companies as Central Government may deem fit.

### **c) Auditor of Holding Company to comment on the true and fair view of each Subsidiary Company**

Since a Holding Company makes significant investment in its subsidiary companies, Committee proposes that there should be provisions for better oversight, especially on financial matters, of subsidiary companies by the Board and the auditor of the holding Company.

The Committee proposes suitable amendments to ensure that the auditor of the holding company be given assurance about the fairness of audit of each subsidiary company by the respective auditors and additionally, the auditor of the holding company may also be empowered to independently verify the accounts or part of accounts of any subsidiary company.

#### **d) Standardisation of qualifications by auditors**

The Committee stresses on the need for a standard format for auditors to provide the impact of every qualification or adverse remark on the company's financial statements for circulation to the Board before the same is passed on to shareholders.

#### **e) Forensic Audit**

There is a proposal to cover specific rules including triggering event for ordering Forensic Audit under the Companies Act, 2013 so as to have uniformity on this across all regulators.

Presently, there is no such provision about forensic audit under the Companies Act, 2013 and such audits are being conducted on the specific directions of regulators or on demand of creditors.

### **4. Explicit restriction on recoding name of trusts on register of members**

Under previous Companies Act, 2013, there was a provision that register of members or debenture holders shall not contain notice of any trust expressly, impliedly or constructively. In same lines, the Committee proposes to have a specific provision under the Companies Act, 2013 to prohibit Companies from recognising a person holding any share upon a trust.

### **5. Recognizing Special Purpose Acquisition Companies (SPACs)**

There is a proposal to have an enabling provision under the Companies Act, 2013 to recognise SPACs and allow entrepreneurs to list a SPAC incorporated in India on domestic and global exchanges.

The Committee also proposes to have relaxations on requirement to carry out businesses before being struck off and providing exit options to the dissenting shareholders of a SPAC if they disagree with the choice of the target company identified.

## **6. Strengthening the National Financial Reporting Authority (NFRA)**

The Committee proposes to widen the investigating powers of NFRA in addition to the matters pertaining to professional or other misconduct.

The Committee also proposed amendment of Companies Act, 2013 for the constitution of a NFRA Fund and the accounts of the proposed NFRA Fund should be maintained in such form as prescribed by the Central Government in consultation with the Comptroller and Auditor General.

## **7. Enabling the distressed companies to issue shares at discount**

With a view to ease out the requirement of raising share capital in distressed companies, it has been proposed that such companies should be allowed to issue shares at a discount to Central Government, State Government or to such class or classes of persons as may be prescribed, notwithstanding the prohibition under Section 53 of Companies Act, 2013. Further, the registered valuers would continue to value such issuances, failing which such issuances would be void.

## **8. Recognizing issuance of Fractional Shares for certain class of Companies**

For the first time in history of the Company law, a proposal for issuance, holding and transfer of Fractional Shares has been proposed for certain class of Companies. The proposal suggests that such shares could only be issued in Dematerialized Form and for Listed Companies such prescriptions may be made in consultation with SEBI.

This will help retail investors who may not have purchasing power to buy a whole share due to high price of a single Unit.

## **9. Mandatory one-year cooling-off period before auditors become directors**

In order to uphold the independence of auditors, it has been recommended to mandatorily insert one year cooling period from the date of cessation of Auditor's office before auditors could be appointed as Directors.

Currently there is no provision under the Companies Act, 2013 prohibiting an auditor from becoming a non-executive director, managing director or a whole-time director in the same company or group of companies, at any point of time after cessation of auditor's office. In case of audit firm structured as partnership/LLP, such a restriction would operate only concerning the partner that audited the Company.

## **10. Mandatory one-year cooling-off period before an Independent Director becomes Managerial personnel**

In the interest for more transparency and accountability, the Committee suggests that there should be provisions under the Companies Act, 2013 for Unlisted Companies, about cooling period before an independent director could be onboarded as Managerial personnel, like in SEBI regulations.

## **11. Digitalization and ease of doing business**

Certain proposals focusing on digitalization and ease of doing business are as follows:

- a) Considering cost effectiveness, the committee proposes to have rules enabling certain class of Companies to serve prescribed documents to members in electronic mode only.
- b) There is a proposal of replacing affidavits with self-declarations with Office of Registrar of Companies, under various provisions of Companies Act, 2013.
- c) The Committee also proposes that Companies Act, 2013 should enable companies to hold general meeting i.e., AGMs and EGMs physically, virtually and



in hybrid mode. As stakeholders believe that these relaxations must remain operational irrespective of the restrictions ensuing from the pandemic.

- d) The Committee is of the view that the requirement of notice period could be reduced where the meetings are held entirely in electronic mode.
- e) A Single consolidated electronic platform may be proposed by the Central Government for the statutory registers to be maintained, stored and updated periodically by the Companies of certain class, so as to bring uniformity and more transparency.
- f) There is a proposal for making rules on conducting electronic enforcement-related actions and adjudication in a more transparent and non-discretionary manner with a proper trail through an electronic platform.
- g) With a view to ease out the restoration of a struck off Company, there is a proposal that the applicant may approach Regional Director, instead of NCLT, if restoration is applied within 3 years of strike off date.

## **12. Changes in provisions governing Vacation of Office of Director**

Section 164 of the Companies Act, 2013 identifies certain specific circumstances wherein a person shall not be eligible for appointment as the director of a Company. Section 164(1) covers cases where disqualification arises from personal incapacity such as unsoundness of mind, insolvency, conviction by a court, etc. On the other hand, Section 164(2) deals with the disqualification of a director on account of lapses made by a Company in filing its annual returns and financial statement or default in repayment of deposits or debentures.

The Committee proposed that vacation of office under Section 167 should be limited to disqualification triggered due to personal incapacity.

**Conclusion:** The Committee suggests very crucial proposals to be added and modified in the Company law and at the same time gives due consideration to ease of doing business, digitalization, ironing out and streamlining various provisions of the Company law with other statutes.

**DISCLAIMER:**

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