

Accounting and Audit Provisions with respect to New Companies Act 2013

Need for the New Act

- Changing Economic and Business Environment
- Alignment with International requirements
- Sophisticated Stakeholders, Higher expectations
- To condense, simplify, rationalize the provisions

Based on Recommendations of Bhaba Committee, 1950	Companies Act, 1956 was enacted	Companies Act, 1913 was repealed
Companies Act, 1956 → Amended 24 times since 1956. Major Changes were in the form of :		
Based on Sachar Committee Recommendations	Companies Amendment Act, 1988	
Based on Eradi Committee Recommendations	Companies Amendment Act, 2002	Companies (Amendment) Bill, 2003

Spirit of the New Act

- **Strengthening corporate governance practices**
- **Emphasis on CSR**
- Greater emphasis on **Investor Protection**
- Higher rigour in **Financial Reporting framework**
- Enhanced **Auditor's Accountability and Independence**
- Ease of restructuring and cross-border mergers for the companies

Structure of Companies Act compared

	Companies Act 1956	Companies Act 2013
Chapters	XIII	<u>XXIX</u>
Sections	658	470
Schedules	XV	VII

Status of notification of Sections of the Act

Consent of Houses on the Companies Bill, 2013	Lok Sabha: Dec 2012	Rajya Sabha: 8 th August 2013
President assent	29th August 2013	Becomes Companies Act, 2013
Companies Act, 2013	Notified on	Effective from
99 Sections	12 th Sep, 2013	Immediately
183 Sections	26 th March, 2014	1 st April 2014
Certain Provisions of Companies Act 1956 continue to remain in force : For details check - General Circular No. 07/2014 dated 01.04.2014		

Companies Act, 2013 (chapters)

Chapter No.	Chapter Name
Chapter I	PRELIMINARY
Chapter II	INCORPORATION OF COMPANY AND MATTERS INCIDENTAL THERETO
Chapter III	PROSPECTUS AND ALLOTMENT OF SECURITIES
Chapter IV	SHARE CAPITAL AND DEBENTURES
Chapter V	ACCEPTANCE OF DEPOSITS BY COMPANIES
Chapter VI	REGISTRATION OF CHARGES
Chapter VII	MANAGEMENT AND ADMINISTRATION
Chapter VIII	DECLARATION AND PAYMENT OF DIVIDEND
Chapter IX	ACCOUNTS OF COMPANIES
Chapter X	AUDIT AND AUDITORS
Chapter XI	APPOINTMENT AND QUALIFICATIONS OF DIRECTORS
Chapter XII	MEETINGS OF BOARD AND ITS POWERS
Chapter XIII	APPOINTMENT AND REMUNERATION OF MANAGERIAL PERSONNEL
Chapter XIV	INSPECTION, INQUIRY AND INVESTIGATION
Chapter XV	COMPROMISES, ARRANGEMENTS AND AMALGAMATIONS

Companies Act, 2013 (chapters)

Chapter No.	Chapter Name
Chapter XVI	PREVENTION OF OPPRESSION AND MISMANAGEMENT
Chapter XVII	REGISTERED VALUERS
Chapter XVIII	REMOVAL OF NAMES OF COMPANIES FROM THE REGISTER OF COMPANIES
Chapter XIX	REVIVAL AND REHABILITATION OF SICK COMPANIES
Chapter XX	WINDING UP
Chapter XXI	COMPANIES AUTHORISED TO REGISTER UNDER THIS ACT
Chapter XXII	COMPANIES INCORPORATED OUTSIDE INDIA
Chapter XXIII	GOVERNMENT COMPANIES
Chapter XXIV	REGISTRATION OFFICES AND FEES
Chapter XXV	COMPANIES TO FURNISH INFORMATION OR STATISTICS
Chapter XXVI	NIDHIS
Chapter XXVII	NATIONAL COMPANY LAW TRIBUNAL AND APPELLATE TRIBUNAL
Chapter XXVIII	SPECIAL COURTS
Chapter XXIX	MISCELLANEOUS

7 Schedules

- Schedule I – Table A to I (on memorandum and articles)
- Schedule II – Useful lives to compute depreciation
- Schedule III – General instructions for preparation of Balance Sheet and Profit and Loss Account
- Schedule IV – Code for Independent Directors
- Schedule V – Managerial Personnel
- Schedule VI – Infrastructural Projects
- Schedule VII – Prescribed CSR Activities

Notified Rules for

Chapter 1- Companies (Specification of definition details) Rules 2014

Chapter 2- Companies (Incorporation) Rules, 2014.

Chapter 3- Companies (Prospectus and allotment of securities) Rules 2014

Chapter 4- Companies (Share Capital and Debentures) Rules 2014

Chapter 5- Companies (Acceptance of Deposits) Rules, 2014

Chapter 6 -Companies (Registration of Charges) Rules 2014

Chapter 7- Companies (Management and Administration) Rules 2014

Chapter 8- Companies (Declaration and Payment of Dividend) Rules 2014

Chapter 9- Companies (Accounts) Rules 2014

Chapter 10- Companies (Audit and Auditors) Rules, 2014

Chapter 11-Companies (Appointment and Qualification of Directors) Rules 2014

Chapter 12- Companies (Meetings of Board and its Powers) Rules 2014

Chapter13 Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014

Chapter14- Companies (Inspection, Investigation and Inquiry) Rules, 2014

Chapter 22- Companies (Registration of Foreign Companies) Rules, 2014

Chapter 27- Nidhi Rules, 2014

Chapter28- Companies (Adjudication of Penalties) Rules, 2014.

Chapter 29- Companies (Miscellaneous) Rules, 2014

New Definitions

New Definitions

- **Promoter [2 (69)]:** A person who
 - Has been named as such in a prospectus or is identified by the company in the annual return or
 - has control over the affairs of the company, directly or indirectly whether as a shareholder, director or ow or
 - in accordance with whose advice, directions or instructions the BOD is accustomed to act (excludes advisor in professional capacity)
- **Key Managerial Personnel [2 (51)]:** CEO/ MD/ manager, company secretary, whole-time director, CFO etc
- **CFO/CEO :** KMP and related party, responsible for FS
- **Nominee Director:** A director nominated by any financial institution or appointed by Govt. or any other person to represent its interests
- **Small Company [2 (85)]:** (not a holding/ subsidiary/ public co), Paid Up capital < 50 lakhs , or Turnover < 2 crore
- **One Person Company:** one person as a member, Person: Natural, Indian

New Definitions

Subsidiary Company [2(87)]: A company which

- controls the composition of the BOD
- exercises/ controls > 50% of **Total Share Capital** either at its own or through subsidiaries
 - Layers of subsidiaries not beyond a prescribed number

Associate Company [2(6)]: A company in which the other company has significant influence. Excludes Subsidiary, Includes JV

Significant Influence means : control of at least 20% of total share capital, or of Business decisions under an agreement

Control [2(27)] includes

- Right to appoint majority of the directors or
- To control the management or policy decision exercisable by person or persons, acting individually or in concert, directly or indirectly
- Including by virtue of shareholding or management rights, or shareholders agreement or voting agreements or in any other manner

Related Party, Independent director (defined later)

Accounts of companies (Chap IX)

Clarification regarding commencement of provisions related to maintenance of books of account

(General Circular 08/2014)

	Maintenance of books of accounts and preparations/adoption/filing of financial statements, Auditor's Report, Board's report etc	To be governed by
A)	For financial years that commenced earlier than 1st April, 2014	Companies Act, 1956
B)	For financial years commencing on or after 1st April, 2014	Companies Act, 2013

Accounts of companies

A) Uniformity of financial year [Sec 2(41)]

- All companies to adopt uniform “financial year” ending on 31 March every year
 - Exemptions: For holding/subsidiary incorporated outside India (which is required to follow a different FY for consolidation of its accounts outside India)
 - Exemptions are subject to approval of National Company Law Tribunal (NCLT)
- Transitional time allowed to comply: 2 years

B) Consolidated financial statement (CFS) [Sec 129]

- To be prepared by all companies with ≥ 1 subsidiaries (over and above their standalone FS)
 - Explains for this section: “subsidiary” includes associates & JVs
- Implications: Private and unlisted companies would be preparing CFS for the first time, Companies with JVs and associates

Accounts of companies

- Definition of '**Subsidiary**'
 - As per 2013 Act: Based on ownership of share capital (which includes preference capital)
 - As per AS 21 on CFS: Based on ownership of voting power
- **C) Under 1956 Act**, material misstatement in accounts whether due to fraud or error is reported as 'prior period adjustment' in the year in which it is discovered.

2013 Act requires Reopening / Restatement of financial statements (sec 130 and 131)

- **Mandatorily:** If an application is made by Central Govt., SEBI, Income-Tax authorities etc. & an order is made by a court or Tribunal
 - *Ground: Fraudulent financial reporting or Mismanaged affairs*
- **Voluntarily :** If an application is made by company and Tribunal approves
 - *Ground: Directors feel that the financial statements and Board Report are non-compliant (restricted to past three years, once in a year)*

PART I — BALANCE SHEET

Name of the Company.....

Balance Sheet as at

(Rupees in.....)

Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
1	2	3	4

I EQUITY AND LIABILITIES**(1) Shareholders' funds**

- (a) Share capital
- (b) Reserves and surplus
- (c) Money received against share warrants

(2) Share application money pending allotment**(3) Non-current liabilities**

- (a) Long-term borrowings
- (b) Deferred tax liabilities (Net)
- (c) Other Long term liabilities
- (d) Long-term provisions

(4) Current liabilities

- (a) Short-term borrowings
- (b) Trade payables
- (c) Other current liabilities
- (d) Short-term provisions

TOTAL**II ASSETS****Non-current assets****(1) (a) Fixed assets**

- (i) Tangible assets
- (ii) Intangible assets
- (iii) Capital work-in-progress
- (iv) Intangible assets under development

(b) Non-current investments**(c) Deferred tax assets (net)****(d) Long-term loans and advances****(e) Other non-current assets****(2) Current assets****(a) Current investments****(b) Inventories****(c) Trade receivables****(d) Cash and cash equivalents****(e) Short-term loans and advances****(f) Other current assets****TOTAL**

PART II – STATEMENT OF PROFIT AND LOSS

Name of the Company.....

Profit and loss statement for the year ended

(Rupees in.....)

Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previo reporting period				
				VI	Exceptional items	xxx	xxx
				VII	Profit before extraordinary items and tax (V - VI)	xxx	xxx
				VIII	Extraordinary items	xxx	xxx
				IX	Profit before tax (VII- VIII)	xxx	xxx
I Revenue from operations		xxx	xxx	X	Tax expense:		
II Other income		xxx	xxx		(1) Current tax	xxx	xxx
III Total Revenue (I + II)		xxx	xxx		(2) Deferred tax	xxx	xxx
IV Expenses:				XI	Profit (Loss) for the period from continuing operations (VII-VIII)	xxx	xxx
Cost of materials consumed				XII	Profit/(loss) from discontinuing operations	xxx	xxx
Purchases of Stock-in-Trade				XIII	Tax expense of discontinuing operations	xxx	xxx
Changes in inventories of finished goods		xxx	xxx	XIV	Profit/(loss) from Discontinuing operations (after tax) (XII-XIII)	xxx	xxx
work-in-progress and Stock-in-Trade		xxx	xxx	XV	Profit (Loss) for the period (XI + XIV)	xxx	xxx
Employee benefits expense		xxx	xxx	XVI	Earnings per equity share:		
Finance costs					(1) Basic	xxx	xxx
Depreciation and amortisation expense					(2) Diluted	xxx	xxx
Other expenses							
Total expenses		xxx	xxx				
V Profit before exceptional and extraordinary items and tax (III - IV)		xxx	xxx				

Depreciation [section 123(2) and Schedule II]

Schedule XIV of the 1956 Act	Schedule II to the 2013 Act
Specified minimum rates of depreciation	Specifies useful lives

- Schedule II to the 2013 Act specifies *useful lives* over which depreciable amount of the assets are required to be systematically allocated
- ‘*depreciable amount*’: cost *less* residual value
- ‘*residual value*’ ordinarily should **not** be > 5% of original cost of the asset
- For companies which are required to comply with AS
 - should disclose a justification if useful lives used $\neq$ prescribed
- Other companies
 - the useful life and the residual value should **not** be higher than prescribed
- For intangible assets, provisions of the AS applies for the time being
- Specifies useful life for some **new** categories of plant and machineries
 - Example: Those used in distribution of power, manufacture of metal etc.

Depreciation

- Component Accounting:
 - Where cost of a **part** of the asset is significant to total cost of the asset and UL of the part $\neq$ UL of remaining asset, *UL of the part shall be determined separately*
- Transition: From 1st April 2014 (date this schedule became effective)
 - Depreciate Carrying Value (CV) of an asset over its remaining UL
 - If UL is nil, adjust the opening Retained earnings with (CV – Residual Value)
- Impact of the newly prescribed Useful lives on depreciation: The number of years over which the cost of the asset would be spread now would be very different compared to 1956 Act.

	1956 Act		2013 Act
General Category	<u>SLM %</u>	<u>100/SLM %</u>	<u>UL prescribed</u>
Plant and Machinery	4.75 % →	21 years	15
Furniture	6.33% →	16	10
Computer	16.21% →	6	3

Miscellaneous

Mandatory Internal Audit [Sec 138, & Rules, 2014] for

- every listed company and for
- every unlisted public company whose
 - Paid up capital $\geq$ Rs 50 crores or O/S deposits $\geq$ Rs 25 Cr Or Turnover $\geq$ 200 Cr or O/S loans/ borrowings $\geq$ 100 Cr or
- Every private companies with
 - Or Turnover $\geq$ 200 Cr or O/S loans/ borrowings $\geq$ 100 Cr
- Internal audit to be conducted only by CAs or CWAs or other professionals decided by the Board
- Scope, Functioning, Periodicity and Methodology of conducting the audit to be formulated by *audit committee*/ board in consultation with *internal auditor* (D.RULES)
- Transition period : 6 months

Books of Accounts : allowed to be kept in electronic form

- This shall remain accessible in India so as to be usable for subsequent reference (D.RULES)

Shares (except sweat equity shares) can not be issued at discount (Sec 53)

Audit and Auditors (Chap X)

Audit and Auditors

- **Rotation:** (Earlier re-appointment at each AGM) [Section139]

- 2013 Act: Appointment not for more than
 - 1 five year term for Individual as auditor
 - 2 five year terms for Firm as auditor

for listed cos, unlisted public cos: PUC $\geq$ 10 crore, for private cos $\geq$ 20 crore, other cos public borrowings/deposits $\geq$ 50 crore

- 5 year cooling period after completion of his previous term
- Incoming auditor associated with outgoing firm (under same network) can not be appointed till the cooling period of outgoing partner is over
- Transition period allowed : 3 years

- **Disqualification stricter (141):** If business relationship with company; Not auditing more than 20 companies , etc.

- **Prohibition on providing specified non-audit services (144)** (directly or indirectly) to the audit client like accounting and book keeping services, internal audit, investment advisory services etc
 - ‘other services’ if any & other than prohibited ones need Board/Audit Committee approval, 1 year transition period

Audit and Auditors

Auditor's Responsibility Statement should cover (Section 143) :

- Whether company has failed to provide any information or explanation, such details & the effect of the same on FS
- Observations, comments on financial transactions and adverse matters
- Qualification or adverse remark on maintenance of accounts
- Adequacy of internal financial controls and operating effectiveness
- Comment on disclosure by the company on the following issues:
 - of the impact of pending litigation on financial position,
 - making of provisions for foreseeable losses on long term/derivative contracts,
 - delays if any in depositing money into IEPF

Every auditor should comply with **Auditing standards** notified by C Govt.

- Fraud:** (143) Any knowledge / information about 'Fraud' to be reported to
- Audit committee /Board immediately seeking their reply within 45 days. Such reply along with his report to be sent to central govt. within 15 days.
 - If there is no reply with 45 days: his report to be sent to central govt.

Auditors Liabilities

If Tribunal is satisfied that an auditor, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud, it may direct the company

- to change its auditors,
- the auditor will be barred for 5 years.
- He will also be liable u/s Sec 447 for fraud **[140 (5)]**
- If the auditor is a **firm**, the liability is that of the firm & any partner involved in fraud,
 - As per Sec147(5): liability whether civil/criminal shall be of the concerned partners and the ***firm jointly and severally***
 - Rules: Criminal liability of the firm (other than fine) will devolve on the partner in fraud.
- **Penalty on default:** Fine of Rs 25,000 to 5 lakhs, If deception wilful: imprisonment upto 1 year, fine Rs 1 lakh to Rs 25 lakhs, Auditors must refund remuneration and pay damages to those affected

Dividends (Chap VIII and Rules)

- Like in the 1956 Act, company should declare dividend out of
 - (a) CY profits after depreciation, (b) Accumulated profits after depreciation,
 - (c) Out of both
 - (d) Out of money provided by govt. in pursuance of any guarantee given
- Unlike in the 1956 Act, Transfer of specified percentage of profits to reserves before declaring dividend **no more mandatory**
- (D. Rules, 2014) If CY profit is inadequate/ absent, dividend can be declared out of surplus /reserves provided
 - dividend rate < average rate of the last 3 years,
 - amount drawn < $\frac{1}{10}$ of (paid up capital + free reserves),
 - amount drawn to be used for setting off the loss of CY before any equity dividend is declared,
 - after such withdrawal the reserves balance not to be < 15% of PU capital,
 - carried over losses and depreciation not provided in PY to be first set off against CY profits

Dividends (Chap VIII)

- If amounts transferred to '**Unpaid Dividend Account**' remains unclaimed for 7 years
 - Transfer the amounts along with relevant shares to Investor Education and Protection Fund (IEPF)
- Companies who **default on repayment of deposits** are barred from declaring dividends on equity shares
- If the company has incurred loss up to the end of the qtr immediately preceding the declaration of interim dividend
 - **Interim dividend** not to exceed the average rate of dividend declared in the preceding 3 years
- **Penalty:** On failure to comply with the section
 - Company: Fine of Rs 5 lakhs to 25 lakhs
 - Every Officer in default : Fine of Rs 1 lakh to 5 lakhs

Directors

Directors: Appointment (149)

- Number of directors : Maximum 15 (earlier 12) (can be increased through special resolution), Minimum: 2 for private and 3 for public
- For every Listed company, & for every other public company with paid up share capital of $\geq$ Rs 100 crores, or turnover $\geq$ Rs 300 crores
 - At least 1 woman director
- For every company: At least 1 director who stayed in India $\geq$ 182 days in PY
- For Listed companies:
 - At least $1/3^{\text{rd}}$ of the total number of directors should be Independent directors
- For Public companies with paid up share capital of $\geq$ Rs 10 crores, **or** turnover $\geq$ Rs 100 crores, **or** O/s loans, debentures and deposits $\geq$ Rs 50 crores
 - Minimum number of independent directors (Rules): at least 2
- If a director absents all board meetings in 12 months: his office would be **vacant**
- (165) Maximum number of directorship: 20, Max in public companies: 10
 - (SEBI Oct 2014: Ind. Dir. to hold Max 7 board positions in listed co. and Max :3 as WTD)

Independent Directors

- Definition** [Sec 149 (6)]: Director other than a MD/ WTD/**nominee** director who has integrity, relevant expertise and experience, who is or was **not a promoter**, is not related to promoters or directors of the company, its holding, subsidiary or associate
- who during the current and 2 preceding years had no **pecuniary relationship**, or none of whose relative had pecuniary relationship $\geq$ 2% of lower of turnover/ total income or Rs 50 lakhs of the company, its holding, subsidiary or associate
- Neither he nor his relative was** : KMP/ **employee** during 3 preceding FY/ Employee or proprietor or partner **of firm of auditors or consultants**/ holds together with his relatives $\geq$ **2% of voting power** / CEO or director of NPO which receives $\geq$ 25% of its receipts from the company or holds $\geq$ 2% of voting power of the company
- **Remuneration (197)**: Only sitting fee, reimbursement of expenses for participation in meetings and profit related commission (**but no stock option**)
 - **Tenure**: Maximum 5 years (can be extended by another term of 5 years subject to special resolution), followed by a cooling off period of 3 years
 - **Code of conduct** given in **schedule IV** for Independent Directors
 - **Liable** for acts or omissions which occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently, a resigning director would be **Liable** for offences if any during his tenure

New Board Committees

For every listed and other Public company with paid up share capital of $\geq$ Rs 100 crores, **or** turnover $\geq$ Rs 100 crores, **or** O/s loans, debentures and deposits $\geq$ Rs 50 crores, the board should form the following committees:

- **Nomination and Remuneration Committee**
 - **Composition:** $\geq$ 3 non-executive directors, out of which half independent
 - **Responsibilities:** To recommend appointment and removal of directors/senior management, To recommend remuneration policy for KMP, directors and carry out evaluation of performance of directors
- **Audit Committee (177 & Rules):**
 - **Composition:** with minimum of three directors, majority should be independent, & majority including its chairperson should have ability to read and understand the financial statements
 - **Responsibilities:** Recommending appointment of auditors and monitoring their independence and performance, examination of FS, approval of related party transactions, scrutiny of inter-corporate loans and investments, valuation of assets of the company, evaluation of internal financial controls, monitoring the end use of funds raised through public offers

Report by the Board of Directors (Section 134)

Content: Report to be on standalone basis with a **separate section** on performance and financial positions of subsidiaries, JVs, associates included in CFS

- Number of Board meetings
- Extract of annual return
- Directors' Responsibility Statement
- Statement on **declaration of independence** by the independent directors,
- Company's policy on director's appointment and remuneration,
- Explanation and comments by Board on qualification, reservation or adverse remark, disclaimer made by Auditor /CS in his secretarial Audit Report
- Particulars of loans, guarantees and investments
- Contracts and arrangements **with related parties** (format in rules),
- Statement on development and implementation of a risk management policy
- Policy developed and implemented by the company on **corporate social responsibility** initiatives taken during the year, vigil mechanism
- Manner in which formal annual performance evaluation of the Board/its committees/ individual directors have been conducted (listed, PUC> 25 cr)

Directors Responsibility Statement (in addition to requirements in 1956 Act) :

- the directors had laid down internal financial controls to be followed by the company and they are adequate and operating effectively
- directors have devised proper systems to ensure compliance with all applicable laws and such systems are adequate and operating effectively

Database on people willing and eligible to be independent directors

- To be created and maintained by a body notified by central govt.
- Database to be placed on MCA website or other website

For companies with ≥ 1000 security holders at any time during the FY, the Board should form a **Stakeholders Relationship Committee**

- Chairperson is Non-executive director
- to resolve the grievances of security holders

Meetings (Schedule IV): Independent directors to hold one annual meeting **without** non-independent director, KMP or Senior Management

Duties : A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment [166 (2)]

Directors

Liability : An independent director Or *a non-executive director not being promoter or KMP* shall be held liable,

- only in respect of such acts of omission or commission by a company, which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance
- or where he had not acted diligently

Disqualifications:

- New Grounds such as convicted of offence dealing with RPT,
- Director identification number not obtained,
- Permanent debarment of director sentenced to jail ≥ 7 years

No loan to directors /other person in whom the director is interested (**Sec185**) (1956 act exempted loan from holding to WOS, Rules partially correct it)

No loan/ investment in a body corporate exceeding 60% of (PUC, free reserves, securities prem) or > 100% of (free reserves, securities prem) without approval through special resolution (1956 exempted loans to WOS, Rules : Exempted for loans to WOS and JV)

Investor Protection

Investor Protection

Prevention of Oppression and Mismanagement [section 241-246]

Class Action suits can be filed

- On company/ its directors/ auditors/ consultants
- For fraudulent, unlawful or wrongful act; or improper or misleading statements
- By 100 or 10% of total number of members/depositors (whichever is lower) or by members (depositors) holding $\geq 10\%$ of issued share capital (total O/S value of deposits)
- Members or Depositors may apply to Tribunal if company conduct is prejudicial to public interest or company interest or prejudicial or oppressive to them
- **Source** of promoter contribution to be disclosed in prospectus, Listed companies to file return on **change in shares** held by promoters/top10 SHs
- **E-voting** : For Listed Company or a Company having 1000 or more SHs, Shareholders can vote in Gen Meetings by electronic means (Sec 108)

Investor Protection

National Financial Reporting Authority (NFRA) (section 132 & 133)

Constituted by Central government (1 chairman + 15 P/F members)

- To recommend, monitor and enforce compliance of accounting and auditing standards, oversee the quality of service of accountants
- Given Quasi judicial powers to investigate matters of professional (or other) misconduct by CAs
 - If proved, can impose fine: Rs 1 lakh to 5 times fees received for individual, Rs 10 lakhs to 10 times fees received for firm, can debar from practice- 6 Months to 10 Years
- When NFRA has initiated investigation in matters of misconduct, any other body doing the same shall stop
- It shall undertake investigation or conduct quality review of audit of :
 - listed companies, unlisted companies (NW $\geq$ Rs 500 crores, PUC $\geq$ Rs 500 crores, turnover $> \geq$ Rs 1000 crores (as on 31st march of PY), companies with securities listed outside India (Draft Rules)

Investor Protection

Prohibitions (section 192, 194 and 195)

- Directors not to buy /sell assets on non-cash basis without proper SH approval
- Director/ KMP to refrain from **forward dealing**/ buy options in shares or debentures of company/ holding company/ subsidiary/ associate
 - Punishment : Imprisonment up to 2 years or fine of Rs 1 –5 lakhs or both
- No director/ KMP with access to non-public price sensitive information to indulge in any form of **insider trading**
 - Punishment : Imprisonment up to 5 years, or fine of Rs 5 lakhs to 25 crores or three times the amount of profits made out of insider trading, whichever is higher, or with both.

Investor Protection

Fraud Risk Mitigation

Fraud (447) : Act, omission, concealment of fact, or abuse of position

- committed with intent to deceive, to gain undue advantage from, or to injure the interests of Comp/its SHs/ its CRs/others, whether or not there is any wrongful gain or loss
- **SFIO** made statutory body: given statutory status & significant powers (including arrest), comprises of experts from various disciplines
- Auditors to report fraud
- For listed and others (with deposits or borrowings $\geq$ 50 crores), **Vigil mechanism (Whistleblower)** to be established mandatorily
 - So that directors/ employees can report their genuine concerns
 - To provide adequate safeguards against victimization of whistleblower
 - Provisions to be made for direct access to Chairman, Audit Committee
- Establishment of such mechanism: To be disclosed in Board's Report, Company's website
- **Penalty** for fraud : Imprisonment: 6 M to 10 years, fine which can extend to 3 times the amount involved in the fraud

Investor Protection

Investor Education and Protection Fund (IEPF) can be used to

- Refund unclaimed dividends, promote investor education, distribute money to investors who suffered losses due to wrong actions by others, reimbursement of legal expenses related to class action suits

Related Party – Defined [2(76)]

- Director/KMP or their relative
- Firm in which a Director, Manager or relative is partner
- Private Company in which a Director or Manager is **a member or director**
- Public Company in which a Director or Manager is a director or holds more than 2% either himself or through his relatives**
- Body Corporate or Person – Company is accustomed to act under their direction (other than Professional Advise)
- Holding, Subsidiary or Associate Company, Subsidiary of a holding company to which it is also a subsidiary
- Senior management including functional heads (D. rules)

Related Party transactions (188)

- **Board approval** required where: transactions are either not in the ordinary course of business/not at arm's length
- **Special resolution** required if Share capital $\geq$ Rs 10 crores, Or RPT exceeds the following threshold limits: (**no member who is related party can vote**)

	Nature of Related Party Transaction	Thresholds (which needs special resolution)
a	Sale, purchase or supply of any goods or materials (directly/ through agents)	> 25% of Turnover
b	Selling or buying, property of any kind (directly/ through agents)	> 10% of Net worth
c	Leasing of property of any kind	> 10% of Net worth or Turnover
d	Availing or rendering of any services (directly/ through agents)	> 10% of Net worth
e	Related party's appointment to any office or place of profit in the company, its subsidiary company or associate company	At monthly remuneration > Rs 2.5 lakhs
f	Underwriting the subscription of any securities or derivatives of the company	Remuneration > 1% of Net worth

Related Party transactions (188)

Penalty for violation:

- Contract may be rendered as void,
- Directors concerned to indemnify the loss,
- Director / employee involved can be fined and imprisoned
 - Listed company: Imprisonment upto 1 year , fine of Rs 25,000 to Rs 5 lakhs or both
 - Others: Fine of Rs 25,000 to Rs 5 lakhs or both

Directors Report to include:

- Details of RPT requiring Board's approval and Special Resolution, along with justifications

Shareholder and Disclosure based regime replaces the earlier government approval based regime for RPTs

Corporate Social Responsibility

Corporate Social Responsibility

(Section 135, Schedule VII & Rules, 2014)

Every company with net worth $\geq$ Rs 500 crores, or turnover $\geq$ Rs 1000 crores or, net profit $\geq$ Rs 5 crores during any FY should form

- **CSR Committee** (with at least 3 member, out of which at least one must be independent). Its responsibility:
 - Formulate CSR policy : Includes list of projects/activities to be undertaken under the purview of Schedule VII and monitoring process
 - recommend amount of CSR expenditure to be incurred on the projects
 - monitor CSR policy from time to time
- **Mandatory CSR reporting:** CSR policy disclosed in the **Board's report** after having approved it (as per annexure in CSR Rules, 2014) (website display)
- **Board** to ensure that the company spends at least **at least 2% of the** average net profits of the company during the 3 immediately preceding FY

Corporate Social Responsibility

- (D.Rules) A Company can conduct CSR activities through registered Trust/ Sec 8 companies not set up by the company itself having 3 years of track record, It can collaborate with other companies
- **Excluded:** CSR activities outside India; for the exclusive benefit of the employees /their families; contribution to political party
- Preference to local area and areas around where it operates
- **Comply or Explain :** If a company fails to spend the amount, it should specify the reasons in Board's report, No penal Provisions
- **CSR Activities as per Schedule VII** includes activities related to :
Hunger, Poverty, education, gender equality, child mortality & maternal health, immunodeficiency diseases, environmental sustainability, vocational skills, Social business projects,
Contribution to the PM's National Relief Fund or other govt. fund for socio-economic development and relief, welfare of SC/ST, minorities, women etc.

Spirit of the New Act

- **Strengthening corporate governance practices**
 - by bringing in greater responsibilities on board, auditors including that of Related party transactions, new committees, internal controls
- **Emphasis on CSR** : Moving to broader stakeholders approach beyond narrow shareholder focus
- Greater emphasis on **Investor Protection**
 - like allowing class action suits, introducing NFRA as independent oversight / regulator for auditor, insider trading prohibitions, empowering SFIO, bringing whistleblower mechanism, maintaining Investor Education and Protection fund
- Higher rigor in **Financial Reporting framework**,
 - lowering threshold for consolidation, and bringing in mandatory internal audit, restatements of financial statements
- Enhanced **Auditor's Accountability and Independence**
 - auditor rotation, stricter disqualification, prohibition on non-audit service, broadening auditors responsibility and severe penal provisions
- Ease of restructuring and **cross-border mergers** for the companies

Challenges Ahead

- Power to remove difficulty has been already used many number of times
- Rules often go a long way away from the Act
- Compliance difficult and costly with numerous disclosure requirements, Is compliance going to be more important than business ?
- Getting directors would be difficult when director liabilities are perceived to have increased significantly
- Putting internal controls in place like protection of assets is difficult to operationalize
- Areas corporates are grappling with: E voting, FY of a JV for CFS

Implications:

1. **For CEO/ CFO/ Company:** Some fast track mergers, but greater difficulty in structuring transactions due to a number of small, disconnected changes, Class Action Liability can bring change in corporate behavior
2. **For promoters & minority SHs power balance:** Empowering of minority SHs (minority exits) is a fundamental change, Promoter are coming to reality that they have to take into consideration the power minority SHs now have
3. **Board and independent directors:** Effectiveness, governance can be expected to improve, ID have found new voice

THANK YOU 😊

GOVERNMENT COMPANIES (Chap XXIII)

Where Central govt. is a member

- CG shall cause preparation of an Annual Report within 3 months of its AGM
- Such AR, CAG's comments and a copy audit report should be laid before both the houses of parliament

Where State govt. is also a member

- SG shall caused copy of such AR, CAG's comments and a copy audit report should be laid before both the houses of State legislature

Where Central govt. is not a member (1 or more state govts are):

- SG shall caused preparation of an Annual Report within 3 months of its AGM
- Such AR, CAG's comments and a copy audit report should be laid before both the houses of State legislature

Accounting Reforms on the Anvil to convert government accounting from traditional cash-based accounting to accrual-based accounting

Restructuring

Restructuring

- **Rationalizing Multilayered Structures**
 - Investments through > 2 layers of investment companies: Not allowed
- **Simplifying Procedures for Merger [section 232]**
 - NCLT to approve schemes of restructuring companies(not High Court)
 - Auditor to certify compliance with Accounting Standard for listed, unlisted and private companies
 - Consent of majority Members/ Creditors >75 percent (in value)
 - Merger of listed company into unlisted company allowed if:
 - Exit opportunity being provided to public shareholders;
 - Valuation done as per SEBI guidelines
- **Minority buy-out [section 236]**
 - acquirer holding ≥ 90 percent share capital can notify and offer buy-out balance equity shares from minority SHs at a price determined by registered valuer (minority SHs can offer to sell the same to majority SHS)

Restructuring

- **Cross-border Merger** [section 234]
 - Merger of Indian company with foreign company and vice-versa now permitted
 - CG & RBI to make necessary Rules, Merger to be approved by NCLT
 - Consideration only in cash or Depositary Receipts
- **Fast-track Merger** [section 233] without NCLT approval possible between
 - Two or more small companies; or holding and wholly owned subsidiary subject to following:
 - Declaration of Solvency required to be submitted by both
 - Needs approval by members owning > 90% of total number of shares and creditors >90% in value

Miscellaneous

- Restricts utilization of securities premium (section 52)
- Preference shares can be issued with a redemption period exceeding 20 years for specified infrastructure projects (Sch VI) (section 55)
- More stringent requirements to enable the company to accept deposits from public (73, 76)
- Requires companies to repay the deposits (including interest thereon) accepted under the 1956 Act within one year from the commencement of this section [74(1)]
- The rate of interest on **inter corporate loans** not to be lower than the prevailing yield of Government security closest to the tenor of the loan.
 - Provisions extended to loan given to any person

Miscellaneous

Buy Back

- Share capital reduction not allowed in companies that have overdue deposit /interest
- No buy-back permitted until 3 years from remedy of the defaults on deposits/ preference shares/term loans
- Multiple buy-back within a year not allowed (i.e. 1 year gap between two buy backs)
- Requires Auditor's certificate and compliance with other conditions
- Penalty on default harsher
 - Company : Fine of Rs1 lakh to Rs 3 lakhs
 - OID: Prison up to 3 years and /or fine Rs1 lakh to Rs 3 lakhs

Clarification : Public Company & Private Company

- **Similarity**
 - Incorporated, So Separate legal entity
 - Limited liability
- **Difference**

Difference	Private	Public
Transfer of shares	Restricts (all shareholders must agree)	No restriction
Minimum Paid up Share capital (Rs)	1 lakh	5 lakhs
Maximum members	200	None
Minimum number of directors	2	3

Form of Abridged Financial Statements

Name of the Company

Abridged Balance Sheet as at

(Rupees in)

		Figures at the end of		
		Current reporting	Previous reporting	
		period	period	
		(DD/MM/YY)	(DD/MM/YY)	
I	EQUITY AND LIABILITIES			II. ASSETS
(1)	Shareholders' funds			(5) Non-current assets
(a)	Paid-up Share Capital			(a) Fixed assets
(i)	Equity			(i) Tangible assets (original cost less Depreciation)
(ii)	Preference			(ii) Intangible assets (original cost less Depreciation/amortisation)
(b)	Reserves and surplus			(iii) Capital work-in-progress
(i)	Capital Reserves (including Revaluation reserve, if any)			(iv) Intangible assets under development
(ii)	Revenue Reserves			(b) Non-current investments
(iii)	Surplus			(c) Deferred tax assets (net)
(c)	Money received against share warrants			(d) Long-term loans and advances
(2)	Share application money pending allotment			(e) Other Non-Current Assets
(3)	Non-current liabilities			(6) Current assets
(a)	Long-term borrowings			(a) Current investments
(b)	Deferred tax liabilities(Net)			(b) Inventories
(c)	Other Long-term liabilities			(c) Trade Receivables
(d)	Long-term provisions			(d) cash and cash equivalents
(4)	Current liabilities			(e) short-term loans and advances
(a)	Short-term borrowings			(f) Other current assets
(b)	Trade Payables			
(c)	Other current liabilities			
(d)	short-term provisions			
Total of (1) to (4)				Total of (5) to (6)

Abridged Profit and Loss Account for the year ended on

(Rupees in)

Sr.No.	Particulars	Figures for the current reporting period(DD/MM/YY)	Figures for the previous reporting period(DD/MM/YY)
I	Income		
	Revenue from operations(details to be given as per *)		
II	Other Income		
III	Total Income(I+II)		
IV	Expenditure		
(a)	Cost of materials consumed		
(b)	Purchase of stock-in-trade		
(c)	Changes in inventories of finished goods, work-in-progress and stock-in-trade		
(d)	Employee benefit expense		
(e)	Finance costs		
(f)	Depreciation and amortisation expenses		

S.No	Particulars	Figures for the current reporting period (DD/MM/YY)	Figures for the previous reporting period(DD/MM/YY)
I	Sale of products manufactured		
II	Sale of goods traded		
III	Revenue from services provided		
IV	Other Operational Revenue		

(g)	Other expenses		
	Total Expenditure (a to g)		
V	Profit before exceptional and extraordinary items and tax (III-IV)		
VI	Exceptional items		
VII	Profit before extraordinary items and tax (V-VI)		
VIII	Extraordinary items		
IX	Profit/(loss) before tax (VII-VIII)		
X	1. Tax expense 2. Deferred tax		
XI	Profit/(Loss) after tax for the period from continuing operations (IX-X)		
XII	Profit/(loss) from discontinued operations		
XIII	Tax expenses of discontinued operations		
XIV	Profit/(loss) from discontinued operations (after tax) (XII-XIII)		
XV	Profit/(Loss) for the year (XI+XIV)		
XVI	Earnings per equity share: (a) Basic (b) Diluted		

THANK YOU 😊