

Welcome relief to closely held companies

Parliament last week cleared the Companies (Amendment) Bill, 2014, which seeks to simplify some provisions of the Companies Act, 2013, to facilitate ease of doing business. Here's what it means for businesses:

PAYMENT OF DIVIDEND

The requirement of setting off lower of past losses and depreciation was not brought forward from the Companies Act 1956 to the Companies Act 2013. As a result, companies were able to distribute dividend from current year profits, without setting off past losses and depreciation. The provision of setting off past losses and depreciation has been introduced. Companies that had unadjusted past losses and declared profits out of current profits in Financial Year 2014-15 will no longer be able to declare dividend going forward, until the past losses are offset.

RELATED-PARTY TRANSACTIONS

Certain material related party transactions covered under Section 188, such as sales, purchases, leasing, and selling of property, required special resolution in the shareholders meeting, and interested related parties were not permitted to vote. Considering the hardship imposed on companies in obtaining special resolution of minority shareholders, the requirement of obtaining a special resolution has been replaced by an ordinary resolution. This amendment will provide a welcome relief to closely held companies that faced a challenge in obtaining special resolution from the non-interested shareholders.

OMNIBUS APPROVALS FOR RELATED PARTY TRANSACTIONS

All related party transactions are required to be approved by the audit committee. The 2013 Act does not specifically permit omnibus approval by the audit committee, while such a provision was included in the amended Sebi Clause 49. Companies may now be able to obtain omnibus approvals for related party transactions since the amendment permits obtaining omnibus approvals from the audit committee.

REPORTING OF FRAUDS BY AUDITORS

All frauds identified by the auditor during the performance of their duties are required to be reported to the Central government. The Act did not provide any materiality thresholds for reporting. The Bill has included an enabling provision for the prescription of a materiality threshold for reporting of frauds to the Central government. The amendment however has also included a requirement to include in the Board Report all the frauds which have not been reported to the Centre. The requirement to disclose frauds in the Board Report is useful information for stakeholders, but may result in sensitive information being made available publicly

UNCLAIMED DIVIDEND

The Companies Act 2013 provided that all shares in respect of which dividend were unpaid or unclaimed be transferred to the Investor Education and Protection Fund (IEPF). The Companies (Amendment) Bill 2014 specifies that the shares are required to be transferred to IEPF only when the dividend is unpaid or unclaimed for a period of 7 years consecutively.

LOANS AND GUARANTEES

Loans by companies to wholly- owned subsidiaries and guarantees by holding company made to banks or financial institutions in respect of borrowings by subsidiaries for their principal business activities were permitted by way of an amendment to the Rules to Section 185. The Companies (Amendment) Bill 2014 now includes the guidance that was earlier included in the Rules in the Act. This change is important as the guidance is now moved to the Act, which is more authoritative.

(Business Standard)