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The Companies (Amendment) Act, 2017

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The Companies (Amendment) Act, 2017

Amendments to the Companies Act, 2013

The Government has proposed to bring about several significant changes/amendments to the Companies Act, 2013 ('Companies Act') pursuant to the Companies (Amendment) Act, 2017 ('Amendment Act') which was passed by the Lok Sabha on July 27, 2017 and the Rajya Sabha on December 19, 2017, and received Presidential assent on January 3, 2018. The provisions of the Amendment Act are being notified in a phased manner. The Ministry of Corporate Affairs ('MCA') has, by way of notifications dated January 23, 2018 and February 9, 2018 ('MCA Notifications') notified, with effect from January 26, 2018 and February 9, 2018, various Sections under the Amendment Act. The other amendments proposed under the Amendment Act, which have not yet come into force, will become effective on such date(s) as the Central Government may notify.

This special edition of *Inter Alia...* sets out, in brief, the key amendments brought about by the Amendment Act and the MCA Notifications notifying certain amendments.

1. **Definition of Associate Company:** Section 2(6) of the Companies Act defines an 'associate company' to mean "a company in which the other company has 'significant influence', but which is not a subsidiary and includes a joint venture company of such company having significant influence". Pursuant to the Amendment Act:
 - i. the definition of the term 'significant influence' has been changed to mean: (i) 20% of the **voting power** instead of 20% of the share capital (which included preferential share capital); and (ii) control of **or participation in** business decision under an agreement (thereby linking participation making rights for business decisions, under an agreement, to determine the influence exercised).
 - ii. a new definition of 'joint venture' has been added, to mean "a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement". The intention has been to align the definition to the meaning assigned under the Indian Accounting Standards (Ind AS 28).
 - This amendment has not yet become effective.
2. **Holding Company:** The definition of a 'holding company' under Section 2(46) of the Companies Act was restricted only to 'companies' of which other 'companies' are subsidiary companies. The term 'company' is defined under Section 2(20) of the Companies Act to include only those companies incorporated under the Companies Act or any previous company law. This resulted in a few discrepancies; for example, it could be argued that a foreign parent is not a holding company/related party under the Companies Act. In order to rectify this anomaly, the Amendment Act has clarified that a holding company now includes 'body corporate'.
 - Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.
3. **Key Managerial Personnel:** The Amendment Act has also widened the meaning of 'key managerial personnel' under Section 2(51) of the Companies Act to include officers, not more than one level below the directors, who are whole-time employees and are designated as key managerial personnel by the Board. This change has been introduced as per the recommendation of the Companies Law Committee ('CLC') Report of February 2016, to provide greater flexibility to companies to designate other whole time officers of the company as key managerial personnel.
 - Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.
4. **Related Party:** The term 'related party', as currently defined, used the word 'company' in Section 2(76), thereby including in its purview only that those entities that were incorporated in India. This resulted in the impression that companies incorporated outside India (such as holding/ subsidiary/ associate / fellow subsidiary of an Indian company) were excluded from the purview of related party of an Indian company. The Amendment Act has rectified this anomaly by substituting the word 'company' with 'body corporate', and has also widened the scope of a 'related party' to include an investing company or the venturer of a company. An 'investing company' or a 'venturer of a company' has been defined to mean "a body corporate whose investment in the company would result in the company becoming an associate company of the body corporate".
 - Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.



5. **Subsidiary:** Similar to the changes proposed to the term ‘significant influence’¹, the definition of the term ‘subsidiary’ under Section 2(87) of the Companies Act is proposed to be revised to link control from ‘total share capital’ (which includes preferential share capital) to ‘total voting power’ (which includes only equity share capital), to ensure that the equity share capital acts as the basis for determining the holding/subsidiary relationship.
 - *This amendment has not yet become effective.*
6. **Effect of Number of Members Falling below Prescribed Threshold:** The Amendment Act has introduced a new provision in the Companies Act, Section 3A, whereby, if the number of members in a company falls below the required number of members (seven for a public company and two for a private company), and the company continues to carry on business for more than six months cognizant of the fact that the number of members is below the statutory minimum, then the members of the company will be severally liable for the payment of the whole debts of the company contracted during that period. This new section corresponds to Section 45 of the Companies Act, 1956.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
7. **Reservation of Name for a Company:** The period for reservation of name provided under Section 4 of the Companies Act has been revised from ‘60 days from date of application’ made by a company to the Registrar of Companies, to (a) ‘20 days from the date of approval’ for new companies, and (b) ‘60 days from date of approval’ for existing companies.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from January 26, 2018.*
8. **Authentication of Documents:** Section 21 of the Companies Act provides that a document requiring authentication by a company, or contracts made by, or on behalf of a company, may be signed by any key managerial personnel or an officer of the company, who has been duly authorized by the Board of directors of the concerned company. The term ‘officer’ under Section 2(59) of the Companies Act only included top level management persons in a company. Therefore, in order to remove the practical difficulty and enable the personnel in-charge of the day-to-day operations to authenticate documents on behalf of a company, the Amendment Act has now permitted any ‘employee’ to sign, provided such employee has been directed pursuant to a Board resolution.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
9. **Change in Contents of Prospectus:** Disclosures in the prospectus required under the Companies Act, and the Securities and Exchange Board of India Act, 1992 (‘SEBI Act’) and the regulations made thereunder are proposed to be aligned by omitting the information requirement under the Companies Act. Accordingly, the amended Section 26(1) states that the contents of the prospectus with respect to financial information and reports on financial information will be specified by the Securities and Exchange Board of India (‘SEBI’) in consultation with the Central Government. Until SEBI specifies the information and reports on financial information under this sub-section, the regulations made by SEBI under the SEBI Act in respect of such financial information or reports on financial information will apply.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
10. **Private Placement of Securities:** The Amendment Act has substituted Section 42 of the Companies Act relating to private placement of securities. The following are the changes:
 - i. To ensure accountability and transparency, a company is prohibited from utilizing the money raised through private placement unless allotment is made and a return of allotment has been filed with the Registrar of Companies (‘RoC’). Further, the time to file the return of allotment with the RoC has been reduced from 30 days of allotment to 15 days of allotment. A new sub-section has been added imposing monetary liability on promoters and directors in case of default.
 - ii. The private placement process is simplified by doing away with separate offer letter details to be kept by company and reducing number of filings to the RoC. Pursuant to the amendment, the Board of directors will identify the select group of

¹ Please see Paragraph 1 above of this Special Edition to note the changes proposed to the term ‘significant influence’.



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- person to whom the private placement offer is to be made and the company will keep a record of such persons. Earlier, a company was required to file a complete record of the offers in the Form PAS-5 with the RoC.
- iii. Since renunciation of rights was being used as a way to bypass the provisions of private placement, it has now been stipulated that a private placement offer letter and application should not carry any right of renunciation.
 - iv. It has been clarified that a company may at any time make more than one issue of securities subject to the cap on the maximum number of identified persons.
 - v. Penalty for the contravention has been changed from *higher* of amount raised through private placement or ₹ 2 crore (approx. US\$307,700), to *lower* of the afore-said amounts.
 - *This amendment has not yet become effective.*
11. **Prohibition on Issue of Shares at Discount:** Earlier, the Companies Act provided that shares could be issued at a discount only in the case of sweat equity shares. Now, pursuant to the Amendment Act, in order to enable restructuring of a distressed company in pursuance of any statutory resolution plan or debt restructuring scheme in accordance with any guidelines or directions or regulations specified by the Reserve Bank of India, the newly introduced Section 53(2A) permits a company to also issue shares at a discount to its creditors, as per the statutory guidelines. Further, the word 'discounted price' has been substituted for the word 'discount' under Section 53(2) to clarify that the Section pertains to issue of shares lower than its *nominal value*.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
12. **Acceptance of Deposits by Companies:** The provisions relating to acceptance of deposits by companies contained in Sections 73 to 76 have been amended as follows:
 - i. **Deposit Repayment Reserve Account:** The requirement for maintaining a deposit repayment reserve account in a scheduled bank has been revised to 20% of the amount of deposits maturing during the following financial year (earlier the requirement was 15% of the amount of deposits maturing during the relevant financial year and the succeeding financial year).
 - *This amendment has not yet become effective.*
 - ii. **Deposit Insurance:** The requirement of obtaining deposit insurance in relation to acceptance of deposits from members has been deleted.
 - *This amendment has not yet become effective.*
 - iii. **Defaulting Companies:** Companies which have made good on a default committed in the past would be allowed to accept deposits after expiry of five years from the remedy of such default.
 - *This amendment has not yet become effective.*
 - iv. **Time Period for Repayment of Deposits:** Time period for repayment of deposits accepted by companies prior to the commencement of the Companies Act has been revised to the earlier of: (i) *three* years from the commencement of the Companies Act; or (ii) on or before expiry of the period for which the deposits were accepted.
 - *This amendment has not become effective yet pursuant to the MCA Notifications.*
 - v. **Penalties:** The minimum fine for contravention of Section 73 (which contains provisions relating to acceptance of deposits from members) and Section 76 (which contains provisions relating to acceptance of deposits from persons other than its members) has been modified from ₹ 1 crore (approx. US\$ 154,000) to the *lower* of ₹ 1 crore (approx. US\$ 154,000) or twice the amount of deposits accepted by the company. Further, the officers in default may be liable for fine as well as punishable with imprisonment.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
13. **Beneficial Interest in Shares:** Earlier, Section 89 of the Companies Act obligated every person acquiring/holding beneficial interest in a share as well as the legal owner to make a declaration to the company in respect of such beneficial interest, and Section 90 provided for investigation of beneficial ownership of shares in certain cases by the Central Government. In order to strengthen the existing machinery to identify the natural persons actually controlling a corporate entity, so as to reduce illegal practices like tax evasion and money laundering through corporate vehicles, the provisions have been amended. The Amendment Act has introduced a definition of 'beneficial interest' and reporting mechanism as follows:
 - i. **Definition of Beneficial Interest:** The proposed definition of 'beneficial interest' is



in line with the definition under the Prevention of Money Laundering Act, 2002 and the definition under circulars and guidelines issued by SEBI from time to time. 'Beneficial interest in a share' "includes, directly or indirectly, through any contract, arrangement or otherwise, the right or entitlement of a person alone or together with any other person to: (a) exercise or cause to be exercised any or all of the rights attached to such share; or (b) receive or participate in any dividend or other distribution in respect of such share".

- ii. **Declaration of Significant Beneficial Interest:** Individuals who, acting alone or together, or through other persons or trusts, hold not less than 25% or such other percentage as may be prescribed, in shares of a company or the right to exercise, or the actual exercising of significant influence or control (as defined in Section 2(27) of the Companies Act), over the company are required to compulsorily make a declaration to the company in this regard. The company is required to maintain a register of interest declared by such individuals and file this return and any changes therein with the RoC. A company will also have the obligation to intimate persons who have a beneficial interest in the company according to the knowledge of the company and seek information under such notice. Upon failure by the persons to whom such notice has been issued, to provide the relevant information, a company also has the power to apply to the National Companies Law Tribunal ('NCLT') to compel such information to be provided. Stringent penalties including liability for fraud have been introduced for violating this section.

■ *These amendments have not yet become effective.*

14. Declaration of Dividend: The Amendment Act prescribes the following key amendments to Section 123 dealing with declaration and payment of dividend:

- i. **Computation of Profits:** Any amount representing unrealized gains, notional gains or revaluation of assets are to be excluded from the computation of profits. Any change in carrying amount of an asset or liability on measurement of the asset or liability at fair values is also to be excluded.
- ii. In case of inadequate profits, dividend can be declared out of the accumulated profits of previous years transferred to *free reserves* (earlier, dividend could be declared out of the *reserves*).
- iii. **Interim Dividend:** It is clarified that interim dividend can be declared from the closure of the financial year till holding of the annual general meeting and such interim dividend can also be declared out of the profits generated in the financial year till the quarter preceding the date of declaration of the interim dividend. However, where the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of the interim dividend, the interim dividend cannot be declared at a rate higher than the average dividends declared by the company during immediately preceding three financial years.

■ *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*

15. Financial Statements: The key changes introduced by the Amendment Act with respect to financial statements of a company, are as follows:

- i. As per the revised Section 129 of the Companies Act, while preparing its consolidated financial statements, a company is required to include 'associate companies' (which now includes joint ventures as well) in addition to its subsidiaries. The consolidated statement will have to be prepared in accordance with applicable accounting standards.
- *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
- ii. Section 130 provides for re-opening of accounts, after due approval from a court or NCLT. A proviso has been added to the section to restrict re-opening of accounts to eight years, unless a contrary direction has been issued by the Central Government.
- *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
- iii. Under the old regime, the chief executive officer ('CEO') of a company was required to sign its financial statement only if he was also acting as a director. However, pursuant to the Amendment Act, a CEO is now mandatorily required to sign the statements even if he is not the director.

■ *This amendment has not yet become effective.*

- iv. In an effort to make the report of Board of directors' more concise, Section 134 has



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been revised to provide that instead of reproducing the disclosures made in the financial statements, as a part of the Board's report, only the web address of the location where the annual return has been placed is to be mentioned in the report. Further, only salient features of the remuneration and CSR policies have to be mentioned in the report if they have been made available on the company's website.

- *This amendment has not yet become effective.*
 - v. As per the revisions prescribed to Section 136, every listed company is required to place on its website the audited accounts of each of its subsidiary. If the subsidiary, being a foreign entity, is not statutorily required to prepare consolidated financial statements under the law of the country of its incorporation, then the holding Indian company is required to place and file with the RoC the unaudited financial statements of such foreign subsidiary on its website. Further, a company has now been permitted to circulate the audited financial statements to its members at a shorter notice with the consent is obtained of members holding majority in number entitled to vote and who represent at least 95% of the paid-up voting share capital of the Company.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
- 16. Appointment of Auditors:**
- i. The requirement of ratification of the appointment of auditor at every annual general meeting has been omitted.
 - *This amendment has not yet become effective pursuant to the MCA Notifications.*
 - ii. Section 141(3)(i) of the Companies Act provides that any person whose subsidiary, associate company or any other form of entity is engaged, on the date of appointment, in rendering services prohibited under Section 144, will be disqualified from being appointed as an auditor. The Amendment Act amends the language of Section 141(3)(i) to clarify that the restriction would apply only if the services were directly or indirectly rendered to the company, its holding company or its subsidiary company which proposes to appoint the auditor.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
 - iii. The Companies Act under Section 147 provides that where an audit is conducted by an audit firm, and it is proved that the partner or partners of the audit firm have acted in a fraudulent manner or abetted or colluded in any fraud, the liability, whether civil or criminal for such action, will be of the partner or partners concerned of the audit firm and of the firm jointly and severally. The Amendment Act provides that the criminal liability will only devolve on partners who acted in a fraudulent manner or abetted it.
 - *Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.*
- 17. Residence Requirement in respect of Directors:** Section 149(3) of the Companies Act requires a company to have at least one director who has stayed in India for a total period of not less than 182 days in the previous calendar year. Based on the recommendations set out in the CLC Report, the requirement of 182 days' stay in India now has to be computed based on the *extant financial year* instead of the previous calendar year, and in the case of a newly incorporated company, this requirement will apply proportionately at the end of the financial year in which such company is incorporated.
 - *This amendment has not yet become effective.*
- 18. Appointment of Independent Directors:** Following changes have been introduced with respect to provisions of an independent director under Section 149:
- i. One of the criteria for selection of an independent directors under Section 149(6) (c) is that such director should have no pecuniary relationship with the company, its holding, subsidiary or associate company, or their promoter or directors, during the two immediately preceding financial years or during the current financial year. However, this requirement was not in harmony with the provisions of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, which prohibit only 'material' pecuniary relationships for disqualifying appointments as independent directors. Accordingly, the Amendment Act has introduced a materiality threshold, such that remuneration as director or transaction not exceeding 10% of a person's total income or such amount as may be prescribed will not be regarded as a pecuniary relationship and will not impair independence.
 - ii. Section 149(6)(d) has been amended with respect to the scope of restriction on a



‘pecuniary relationship or transaction’ entered by a relative and has been made more specific by clearly categorizing the types of transactions. For example, holding of any security of/interest in the company, indebted to the company, etc.

iii. Currently, an individual is prohibited from being appointed as an independent director if such person or his or her relative is/was a key managerial personnel or an employee in the company, its holding, subsidiary or associate company during any of the preceding three financial years. The Amendment Act has provided that this restriction will not apply if the relative was merely an employee during the preceding three financial years.

▪ *This amendment has not yet become effective.*

19. Disqualification & Vacation of Office of Directors: Pursuant to the Amendment Act, it has been clarified that when a director is appointed in company, which is in default of filing of financial statements or annual return or repayment of deposits or payment of interest or redemption of debentures or payment of interest thereon or payment of dividend, then such director shall **not** incur the disqualification for a period of six months from the date of his appointment. This allowance was made to avoid the paradoxical situation under the Companies Act wherein if a company has not made the requisite filings, all its directors, including new directors, would automatically be disqualified from being directors. Further, once the director incurs disqualification under section 164(2) due to above grounds, then such director would be required to vacate office in all the companies other than the company which is in default.

▪ *This amendment has not yet become effective.*

20. Constitution of the Audit Committee and Nomination and Remuneration Committee: In order to do away with any confusion regarding the requirement of a private company whose debt securities are listed on a stock exchange to constitute any committee, the Amendment Act has clarified that listed public companies (instead of all listed companies) are required to constitute an Audit Committee and Nomination and Remuneration Committee.

▪ *This amendment has not yet become effective.*

21. Loans to Directors and Interested Persons: Section 185 of the Companies Act currently imposes a complete embargo on companies from granting loans, advances etc. to directors and/or provision of guarantee or security for the benefit of directors, and/or persons in which a director is interested. In order to address the difficulties being faced in genuine transactions, this Section has now undergone an overhaul pursuant to the Amendment Act. The key changes introduced are summarized below:

i. Under the Companies Act, the following persons were, *inter-alia*, deemed to be persons in whom director of a lending company was interested: (a) any firm in which a director or relative of a director of the lending company is a partner; and (b) director or relative of a director of the holding company of such lending company, thereby restricting any loans or security to be provided by the lending company to the firm and such director or relative of the director of the holding company. However, pursuant to the Amendment Act, these are not deemed to be persons in whom director of a lending company is deemed to be interested.

ii. Relaxations have been made to the general rule contained in Section 185, by permitting grant of loans and advances and provision of security by a company to a person in whom a director is interested, subject to prior approval by way of a special resolution in a general meeting and the utilization of the loan being restricted to principal business activities of the borrowing entity. Additional penal provisions have been introduced for every officer in default.

▪ *This amendment has not yet become effective.*

22. Related Party Transactions: Following are the key amendments to Section 188 of the Companies Act:

i. Earlier, no member of the company was entitled to vote on an ordinary resolution in connection with a related party transaction, if such member was a related party. Challenges were faced by closely held companies in complying with this requirement. To address this issue, the Amendment Act states that a company, wherein 90% or more members in number are relatives of the promoter or are related parties, all shareholders will be entitled to vote on the ordinary resolution.

ii. Section 188(3) provided that where a related party transaction entered into by the company without obtaining the necessary consent of the Board and/shareholder approval, was not ratified subsequently within three months from the date on which such transaction was entered into, then such transaction would be voidable at the



option of the Board and that the concerned directors would indemnify the company against any loss incurred by it. The Amendment Act states that, in addition to the above, such a transaction would also be voidable at the option of the shareholders.

- Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.

23. **Managerial Remuneration:** Currently, pursuant to Section 197, the total managerial remuneration payable by a public company should not exceed 11% of the net profits of the company for that financial year. The limits could be exceeded with the approval of the shareholders and the Central Government, subject to Schedule V of the Companies Act. The Amendment Act clarifies the following with respect to payment of managerial remuneration:
- The requirement of obtaining Central Government approval for exceeding the current threshold limits under Schedule V for payment of managerial remuneration has been done away with.
 - If the company has defaulted in payment of dues to any bank or public financial institution or non-convertible debenture holders or any other secured creditor, the prior approval of the bank or public financial institution concerned or the non-convertible debenture holders or other secured creditor, as the case may be, is also required to be obtained before obtaining the approval of shareholders in the general meeting.
 - The statutory auditor of the company is now required to make a statement as to whether the remuneration is being paid by the company to its directors is in accordance with the provisions of Section 197, and whether remuneration paid to any director is in excess of the limit laid down under this section and give such other details as may be prescribed.

- This amendment has not yet become effective.

24. **Amendments in respect of Foreign Companies:** Currently, a foreign company in which not less than 50% of the paid-up share capital (whether equity or preference or partly equity and partly preference) is held by one or more citizens of India or one or more companies/bodies corporate incorporated in India, whether singly or in the aggregate, such a company is required to comply with the provisions of the Companies Act, as if it were a company incorporated in India. The Amendment Act clarifies that Sections 380 to 386 (provisions relating to documents to be submitted by foreign company, accounts of foreign company, etc.) and Section 392 (punishment for contravention) and Section 393 (company's failure to comply with provisions of chapter applicable to foreign company not to affect validity of contracts, etc.) would be applicable to all foreign companies. However, pursuant to the revised Section 379, the Central Government may exempt any class of foreign companies from compliance with any of the provisions of Sections 380 to 386 and Sections 392 and 393 of the Companies Act.

- Pursuant to the MCA Notifications, this amendment has come into effect from February 9, 2018.

25. **Delayed filing fee:** Section 403 of the Companies Act allows a company to file documents belatedly up to 270 from the due date for filing, subject to payment of additional fee. This framework has been specifically mentioned for filings under Section 89 (filing of declaration of beneficial interest), Section 92 (filing of Annual Return), Section 117 (filing of resolutions and agreements), Section 121 (annual general meeting report for listed companies), Section 137 (filing of financial statements) and Section 157 (company to inform DIN of directors to ROC). It was observed that the provision was leading to low level of statutory filings within the initial specified period. Therefore, the Amendment Act has removed this condonation period of 270 days.

However, the Amendment Act further provides where any filing is required to be made under Section 92 (filing of Annual Return) or 137 (filing of financial statement), such filing can be made after expiry of the specified period, on payment of such additional fee as may be prescribed, and such fee shall not be less than ₹ 100 (approx. US\$ 1.5) per day and different amounts may be prescribed for different classes of companies. In case of filings other than under Sections 92 or 137, the filings can be made after the prescribed time subject to payment of additional fee as may be prescribed and different fees may be prescribed for different classes of companies. The delayed filing fee has been also linked to the number of defaults. Further the Amendment Act provides that the officers of the company, who are in default, will be liable to punishment, without prejudice to the liability for the payment of fee and additional fee.

- This amendment has not yet become effective pursuant to the MCA Notifications.



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Bloomberg's Global M&A, Legal Rankings Q1 2018

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