

Decoding the New Companies Act

BOARDROOM RULES A new company law has come into effect from April 1. HT takes a look at the finer details:

When did Parliament pass the new Companies Bill?

The Parliament last year had passed the Companies Bill enacting a new framework that will redefine India's corporate governance norms, grant shareholders with greater powers to defend their rights and lay down rules for companies to spend on welfare activities under the broad head of corporate social responsibility (CSR).

How will the new legislation prevent corporate frauds?

The new law imposes checks and balances to prevent frauds, make corporate board room decisions transparent and hold auditors and directors more accountable. Companies will have to rotate auditors after every four years similar to public sector enterprises and banks. Mandatory rotation of auditors would prevent promoters and auditors to unite to doctor books of accounts. Besides, a cap of five years has been put for any person to serve as independent director on a company's board. An independent director cannot serve on the board of the same company for more than two consecutive terms. This will prevent influencing of independent directors to push through promoters' interests. At least a third of a company's board should comprise of independent directors and at least one of the board members should be a woman, according to the new law. The Bill also contains provisions defining rules for inter-corporate loans and norms for creation of a web of step-down sister companies or subsidiaries. The legislation, which has been in the works for several years, will allow creation of special courts for speedy trials — an assurance to investors that cases will not linger on.

What does the Bill say about corporate social responsibility?

For the first time in India, norms for spend on corporate philanthropy has been defined in law. Every company with a net worth of at least ` 500 crore, or minimum turnover of ` 1,000 crore or net profit of at least 5 crore in a year will have to have spend 2% of its average profits of three years on CSR. Every company having a net worth of at least ` 500 crore, or a turnover of at least ` 1,000 crore or a net profit of at least ` 5 crore during any financial year shall constitute a Corporate Social Responsibility Committee of the board consisting of three or more directors. This committee shall formulate and recommend to the board, a Corporate Social Responsibility Policy, which shall indicate the activities to be undertaken by the company. The committee will also recommend the amount of expenditure to be incurred on CSR activities, monitor the Corporate Social Responsibility Policy of the company from time to time. The board will have to spell out the reasons if a company fails to spend the specified amount on CSR.

What does the new law stipulate about the SFIO?

The new legislation, which replaces the 57-year old Companies Act 1956, empowers the Serious Fraud Investigation Office, an agency mandated to investigate corporate scams, with a statutory status armed with the authority to impose punitive measures and in specific instances, even arrest persons found guilty of corporate crimes.

What specific measures are there to empower small shareholders?

The law will allow shareholders' associations to take legal action against promoters and management through 'class action suits'. A class action is a form of lawsuit where a large group of people collectively bring a claim to court. This acts as a deterrent for carrying out a fraud. (see De-Coded). Minority shareholders of up to 10% will have the dissenters' right, can ask the management to buy them out completely.

How will the new law aid self regulation ?

It will aid self-regulation with greater disclosure levels as opposed to the existing "government-approval-based regime", which is seen as restrictive limiting entrepreneurial growth. New forms of organisation such as 'one person-company' and 'small company' concepts would get appropriate legal recognition making India's business law environment more contemporary.

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