



## 'Companies would need to ascertain their cost competitiveness for their survival'

*Interview of Mr B B Chatterjee, Executive Vice President & Company Secretary of ITC Limited on the new Companies Act, 2013*

### **MA** How would the new Companies Act, 2013 protect the interests of minority stakeholders?

The Companies Act, 2013 has some provisions which protect minority stakeholders' interest. Section 245 of the Companies Act, 2013 empowers shareholders and depositors to file class action suits against companies and management in the event they are of the view that the affairs of the company are being mismanaged and the interest of the

minority stakeholders are not being taken care of. However, at least 100 members / depositors or 10% of the total number of members/depositors whichever is less or members/depositors who hold not less than 10% of the total share capital or total outstanding deposits will need to support this initiative. Class action suits can be filed with the NCLT (National Company Law Tribunal).

Section 188 of the Companies Act, 2013 provides that

related party transactions which are not in ordinary course of business or which are not on arm's length basis would require shareholders approval by way of special resolution. Where related party transactions which benefit only one of the parties is proposed to be entered, such interested party will not be permitted to vote when the special resolution is taken up at a general meeting. In other words 75% of the non-interested shareholders would need to approve the special resolution for the company to enter into such transaction. This provision in the new Companies Act also would protect minority interest in some measure.

In cases of mergers or amalgamations involving a listed company as the transferor company and an unlisted company as the transferee company, minority or dissenting shareholders will now be required to be given an exit opportunity at the fair value as provided in Section 232 of the Companies Act, 2013. The fair value will also need to be determined through a valuation exercise.

**MA Would the new Companies Act facilitate domestic and cross-border Mergers and Acquisitions? Would it help the foreign investor?**

Presently, in terms of Section 391 and 394 of the Companies Act, 1956, only foreign companies can merge with Indian companies. Now, Section 234 of the new Companies Act specifically permits mergers & amalgamations between Indian companies and foreign companies with the prior approval of the RBI; the procedure has also been simplified. Moreover, merger of holding company with its wholly owned subsidiaries, and between two or more small companies have also been simplified through confirmation by the Central Government. Such matters for other companies will require approval of the NCLT.

**MA Would the revised accounting standards in the new Act give a true and fair view of business activities?**

The revised accounting standards have not yet been prescribed. In the interim, the existing accounting standards will continue to apply.

The Companies Act, 2013 aims at disclosure of true and fair value of business affairs of a company through mandating preparation by holding companies of consolidated financial statements for all its subsidiaries, associates and joint-venture companies. The scope of disclosures in Directors' Report has also been enhanced.

**MA Would 'The National Financial Reporting Authority' (NFRA) be the supreme authority in accounting standards and audit? What would be its jurisdiction?**

The responsibility of NFRA (to be set up by MCA) in terms of Section 132 of the Companies Act, 2013, would be to lay down the accounting and auditing standards and policies in consultation with the Institute of Chartered Accountants of India. NFRA would oversee the quality of service of professionals associated with ensuring compliance with accounting and auditing standards. NFRA has also been empowered to investigate into complaints of professional misconduct committed by Chartered Accountants. Where NFRA steps in, no other institute or body is permitted to initiate or continue any separate proceedings. In terms of the draft Rules, NFRA may conduct investigation against (a) auditors conducting audit of 200 or more companies in a year or 20 or more Listed companies (b) companies having net worth / paid up capital of Rs 500 crores or more or turnover of Rs. 1000 crores or more, and (c) companies whose securities are listed outside India. Moreover, Section 132 of the Companies Act, 2013, empowers NFRA to impose penalties and debar Chartered Accountants for periods ranging between 6 months to 10 years, if found to be at fault.

**MA When are the draft Rules expected to be published?**

Four tranches of the draft Rules have already been put up on the MCA website for public comments. The last dates for the two of them are already over and for the other two the last dates for public comments are near. I expect the draft Rules to become applicable from April, 2014. Some Rules, however, may be made applicable even earlier; the same way 98 Sections were notified effective 12th September, 2013.

**MA Would the scope of audit be enhanced in both the manufacturing and private sectors after the new Companies Act, 2013 comes into force?**

Internal audit is getting mandated as per Section 138 of the Companies Act, 2013 which requires prescribed classes of companies to conduct internal audit of their operations. Further, with the mandatory requirement of rotation of auditors, the opportunities for other audit firms are expected to get enhanced.

**MA Do you feel that enhancement in cost management techniques is the only solution for the Government, the economy and society?**

In the competitive market scenario, the need for cost determination and cost management is imperative. The maintenance of Cost Accounting Records for most of the products and Cost Audit are being made mandatory. Besides, energy conservation and technology absorption are required to be reported in the Directors Report. Moreover, companies for their survival would need to ascertain their cost competitiveness vis-à-vis their peer group.

**MA What is the benefit of the concept of the One-Person Company? Could you elaborate on this?**

In line with global corporate laws, the Companies Act, 2013 has permitted One-Person Companies to be incorporated. In other words, a single person can now incorporate a company and take the benefit of limited liability. Besides, such a company will have a separate and distinct legal identity under the new Companies Act. There will be fewer regulatory compliances necessary for such companies and costs accordingly will also be lower. For example, a One-Person Company need not hold Board or Annual General Meetings. However there has to be one Subscriber and Director and the name of the successor has to be specifically stated in the Memorandum of Association of the One-Person Company.

**MA Would the scope of Independent Director be enhanced after the implementation of the new Companies Act, 2013?**

The scope of Independent Director will now become more focused under the Companies Act, 2013. Schedule IV specifically lays down a Code of Conduct for the Independent Directors which include the following:

*Guidelines for Professional Conduct for Independent Directors*

- Uphold ethical Standards of Integrity and Probity
- Work in a bona fide manner in interest of the company
- Devote sufficient time and attention
- Not abuse his position to the detriment of the company

*Roles and Functions of Independent Directors*

- The roles and functions are very specific and would include scrutiny of management performance vis-à-vis plans.
- Satisfy that the integrity of financial information, controls & systems of risk management are robust
- Balance conflicting interest of stakeholders.

*The Duties of Independent Directors would envisage*

- Taking appropriate induction and refreshing skills
- Seeking clarification and professional advice as necessary
- Attending all meetings as far as possible and participating constructively and not unfairly obstructing functioning of the Board / Committees

Moreover, the duties of all categories of Directors have now been provided in the new Act itself as is evident from Section 166 of the Act. This is, however, in line with the UK Companies Act, 2006.

**MA How does the new Companies Act, 2013 enhance the scope of function of the Cost Auditor?**

**'CORPORATE GOVERNANCE ENTAILS MANAGING THE BUSINESS OF THE COMPANY IN THE BEST INTERESTS OF THE COMPANY AND ITS STAKEHOLDERS. THE NEW ACT REINFORCES SHAREHOLDER DEMOCRACY, SEEKS GREATER TRANSPARENCY AND ENHANCED ACCOUNTABILITY TOWARDS STAKEHOLDERS, FOSTERS ENTREPRENEURSHIP AND GROWTH, FURTHERS E-GOVERNANCE AND IS EXPECTED TO ENCOURAGE SELF-REGULATION'**

Section 138 of Companies Act, 2013 specifically requires prescribed classes of companies to conduct internal audit of their operations. In this case the qualification of the internal auditor has been left open. The areas of internal audit have also been widened to include operations, finance, cost, management, energy etc. depending on what the Board considers important for the company. The sectors where cost audit will be mandatory have not yet been put up in public domain. Cost audit was initially introduced by the Government for sectors which were provided with subsidies, for example, newsprint. However, cost determination, as I had said earlier, is becoming critical for companies to remain competitive. As a word of caution, the duties and responsibilities of statutory auditors will also be applicable to Cost Auditors.



**MA** The good news is that the new Companies Act, 2013 has made certain rules for certain companies on CSR spending. Do you think that this will help the growth of CSR or will it be perceived as an extra burden?

Companies with a net worth of Rs. 500 crore or more or turnover of Rs. 1000 crore or more or net profit of Rs. 5 crore or more will be mandatorily required to spend at least 2% of their average net profits (PBT) of preceding three financial years on CSR. Preference needs to be giv-

en to spends in and around local areas where the company operates and for causes like promotion of education, promotion of gender equality, empowering women, reduction of child mortality, improvement of maternal health, ensuring environmental sustainability. Considering the causes for which CSR spend is being mandated, in my view industry may not complaint about it. However, a mandated spend being akin to tax finds resistance, particularly since it is the primary responsibility of the Government to take care of well-being of its citizens. Again, one must not forget that the levy of Education Cess continues.

**MA** How would the new Companies Act, 2013 affect Corporate Governance?

Corporate Governance entails managing the business of the company in the best interests of the Company and its stakeholders. The new Act reinforces shareholder democracy, seeks greater transparency and enhanced accountability towards stakeholders, fosters entrepreneurship and growth, furthers e-governance and is expected to encourage self-regulation.

**MA** Any other relevant issues regarding the new Act, 2013?

Fairness and equity demand that when one seeks a poll at a general meeting or sends notice to a company for standing for directorship or objects to a merger or amalgamation, he or she should have a reasonable stake in the company. In other words, the person's interests or rights in some measure is expected to be affected for the person to seek such poll or send such a notice to the company. The new Act, keeping this basic principle in mind, has therefore enhanced the shareholding requirement for demanding a poll and the deposit for standing for directorship. Objections to mergers and amalgamations can now be made only by persons holding more than 10% shares or having an outstanding debt of more than 5% of the total debts of the company.

The criteria for determining sickness has also been changed to provide that a company will be classified as a sick company on its failure to pay more than 50% of its secured creditors, rather than erosion of its entire equity capital as provided in the Sick Industrial Companies (Special Provisions) Act, 1985.

The last area I would draw attention to would be to the definition of subsidiary company which requires holding of more than 50% of the total capital as against voting capital under the present Companies Act. To put simply, a company can keep on changing its subsidiary status if the provider of its preference capital (which is essentially loan funding) keeps on changing. **MA**