

# SAMVĀD: PARTNERS

July 20, 2017

## FURTHER EXEMPTIONS TO PRIVATE COMPANIES

The Ministry of Corporate Affairs on June 13<sup>th</sup>, 2017 issued a Notification no G.S.R. 501 (E) granting further exemptions to private companies (“**Notification**”). This Notification has been issued amending the provisions of Notification no G.S.R. 464(E) dated the 5<sup>th</sup> June, 2015 (“**Principal Notification**”), with the intention of removing unnecessary regulatory hurdles and offering some procedural flexibility for private companies, especially for start-ups. However, these relaxations brought about by the Notification are only applicable to those private companies which have not committed a default in filing its financial statements under section 137 of the Companies Act, 2013 (“**Act**”) or annual returns under section 92 of the Act with the Registrar of Companies.

### Regulatory relaxations introduced by the Notification:

The key changes brought about by the Notification have been listed below:

#### 1) **Meetings of the Board:**

Per the terms of the Notification, a private company which is a start-up is exempt from holding quarterly board meetings. Previously, only one person companies, small companies and dormant companies were given this exemption from holding quarterly board meetings. Now in addition to these companies, start-ups have also been given this benefit. However, these companies still have to have at least two board meetings in a calendar year and the gap between the two meetings should not be less than 90 days.

The term Start-up has been defined in the Notification no G.S.R. 501 (E) dated May 23<sup>rd</sup>, 2017 issued by the Department of Industrial Policy and Promotion (“**Start-up Notification**”). According to the Start-up Notification, an entity will be considered a start-up: (1) if it is a private limited company, partnership firm or a limited liability partnership in India; (2) if it is within the first seven years from the date of its incorporation/ registration (An exception to this is start-ups in the biotechnology sector, for which the period is up to ten years); (3) if its turnover for any of the financial years has not exceeded Rupees 25 crores; and (4) if it is working towards innovation, development or improvement of products or processes or services, or if it is a scalable business model with a high potential of employment generation or

wealth creation (“**Start-up**”).

2) **Quorum for board meetings:**

According to the previous framework, if the number of interested directors, as per the meaning in section 184 (2) of the Act, exceeds or is equal to two-thirds of the total strength of the board of directors, only the directors who are not interested and present at the meeting could be counted for quorum, provided the number of such directors is not less than 2. Now, a new exemption has been introduced for private companies whereby interested directors may be counted as quorum for board meetings, provided they disclose their interest to the board beforehand. This amendment is a welcome change as initially there was no clarity on how quorum would be counted for a board meeting if there were only two directors in a company out of which one was an interested director.

3) **Financial Statement:**

According to section 2 (40) of the Act, the definition of the term financial statement in relation to a company includes a cash flow statement. The proviso to this definition excludes the cash flow statement for all one person companies, small companies and dormant companies. Now, the Notification has excluded Start-ups as well from including the cash flow statement. In order to avail of this exemption, the start-ups have to be recognised as such in terms of the Start-up Notification.

4) **Acceptance of Deposits:**

According to the Act, there is a prohibition on companies from accepting deposits from the public, except in the manner provided under Section 73 of the Act. According to section 73 (2), a company may accept deposits from its members only upon complying with the conditions mentioned therein, such as (1) issuance of a circular showing the company’s financial position to its members; (2) filing a copy of the said circular with the registrar of companies within 30 days; (3) providing deposit insurance., etc. Initially, the Principal Notification had exempted private companies from complying with these conditions, provided that (1) the deposit did not exceed 100% of its aggregate of paid-up capital and free reserves, and; (2) the details are filed with the registrar of companies.

The exemption provided under the Principal Notification has now been substituted. This exemption is now available only to private companies which fulfil the following criteria:

- a. the amount accepted from members does not exceed 100% of the aggregate of paid-up capital, free reserves and securities premium

account. It must be noted here that the term “*securities premium account*” is a new addition in order to make the language of the Notification consistent with the Companies (Acceptance of Deposit) Rules, 2014, as the Principal Notification only exempted private companies if the monies accepted did not exceed 100% of the aggregate of paid-up capital and free reserves. The addition of “*Securities Premium*” has been made to resolve the conflict in the language in the Principal Notification and the Companies (Acceptance of Deposit) Rules, 2014.

- b. a Start-up, for 5 years from the date of its incorporation. This provision brings about a slight variation from the definition in the Start-up Notification. According to the Start-up Notification, a company will be termed as a Start-up as long as it is within the first seven years of its incorporation. However, under this provision, a private company is eligible to the exemption only if it is a private company which is a start-up within the first 5 years of its incorporation. It does not include the extended period of 7 years in terms of the Start-up Notification.
- c. a private company which fulfils all of the following conditions:
  - i. it is not an associate or subsidiary of another company;
  - ii. if its borrowings from banks, financial institutions or body corporate is less than twice of its paid-up capital or INR 500 million, whichever is lower; and
  - iii. there is no subsisting default in repayment of such borrowings.

Private companies fulfilling the abovementioned conditions and accepting deposits from its members have to file the details with the Registrar of Companies.

## 5) **Annual Return:**

According to section 92 (g) of the Act, every company has to prepare an annual return showing the remuneration of directors and key managerial personnel. Per the terms of the Notification, for private companies which are small companies, the annual return need include only the aggregate amount of remuneration drawn by directors and not by key managerial personnel.

Furthermore, in the case of a private company which is a Start-up, the annual return can be signed by the director of the company, in case there is no company secretary.

6) **Auditor's Report:**

According to Section 143 (3) (i), an auditor's report should include whether the company has adequate financial controls system in place and the operating effectiveness of such controls. Now, the Notification has exempted this requirement for private companies fulfilling the following criteria:

- i. a one person company or a small company; or
- ii. a turnover of less than Rs. 50 Crores as per the latest audited financial statement; or which has aggregate borrowings of less than Rs. 25 Crores, from banks, financial institutions, or any body corporate, at any point of time during the preceding financial year.

***\*This is an update for general information purposes only and does not constitute legal advice. Please contact us if you require further clarifications on this subject.***



**Ms. Nivedita Nivargi**

Partner, Bengaluru

[nivedita@samvadpartners.com](mailto:nivedita@samvadpartners.com)



**Ms. Bhadra Menon**

Associate, Bengaluru

[bhadra@samvadpartners.com](mailto:bhadra@samvadpartners.com)

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**BENGALURU CHENNAI HYDERABAD MUMBAI NEW DELHI**

[www.samvadpartners.com](http://www.samvadpartners.com)