The Companies (Amendment) Bill, 2020: Decriminalizing offences under the Companies Act, 2013

Since the advent of the Companies Act, 2013 (the "**Act**"), the governmental authorities in India have often adopted a proactive approach, and proposed and implemented various measures to facilitate ease of doing business for companies operating in India. An onerous vestige of its predecessor legislation which continues in the Act are criminal sanctions that can be imposed in case of minor, technical or procedural non-compliances under the Act.

Therefore, with an objective to rationalise the punishments prescribed under the Act, 16 (sixteen) offences were recategorized into civil defaults pursuant to the enactment of Companies (Amendment) Act, 2019 ("**CAA 2019**") by the Indian legislature. Not long after the CAA 2019 was notified[1], the government sought to introduce further reforms in this direction as part of the Companies (Amendment) Bill, 2020 (the "**CAB 2020**"), pursuant to which further decriminalization of 54 (fifty four) compoundable offences under the Act has been proposed.

CAB 2020 was tabled in the lower house of the Indian Parliament, the Lok Sabha, on March 17, 2020. While the Parliament was adjourned *sine die* on March 23, 2020 on account of the COVID-19 pandemic and the consequent lockdown, the governmental authorities have been implementing measures such as the Fresh Start Scheme that are consistent with the spirit of CAB 2020. In fact, recent news reports have indicated that the Government is keen to expeditiously implement the amendments proposed in CAB 2020 including by way of promulgating an ordinance, if required.

In this note, we discuss various continuing efforts of the Indian governmental authorities towards streamlining the processes for dealing with certain non-

[1] Section 21 of the CAA 2019, amending provisions related to corporate social responsibility under the Act, is yet to be notified

compliances and analyze if the critical changes proposed by CAB 2020 for further decriminalization of offences and alteration of penalties under the Act is a step in the right direction.

FRESH START SCHEME

On March 30, 2020, the Ministry of Corporate Affairs (the "**MCA**") introduced the Companies Fresh Start Scheme, 2020 (the "**Fresh Start Scheme**"), a limited duration scheme available between April 1, 2020 and September 30, 2020, which provides relief by way of condonation of delays in filing of various statutory forms with the Registrar of Companies in India (the "**RoC**") for certain categories of companies.

Companies desirous of availing benefits under the Fresh Start Scheme have an opportunity to complete their outstanding compliances, regardless of the duration of the default without incurring any fine for the delay by merely making a corrective filing together with payment of a one-time filing fee. The Fresh Start Scheme is also available in cases where the concerned RoC may have already launched or has sufficient cause to launch a prosecution against a company and provides immunity from penal proceedings which such delay or non-compliance(s) could have otherwise attracted.

Although the Fresh Start Scheme was part of the retinue of spontaneous reforms announced by the Ministry of Finance on March 24, 2020 i.e., immediately before the pandemic related lockdown commenced, it is illustrative of the Indian government's long term strategy to promote the ease of doing business in India.

IN-HOUSE ADJUDICATION FRAMEWORK

The In-House Adjudication Mechanism under Section 454 of the Act (the "**IAM Framework**") was one of the key amendments introduced by CAA 2019 to alter the manner in which certain compoundable offences under the Act are dealt with. The IAM Framework substituted the process of appeal and adjudication before the National Company Law Tribunal ("**NCLT**") with an online platform administered by the MCA in relation to certain identified offences.

Pursuant to the IAM Framework, an adjudicating officer ("**AO**") has the power to settle offences by charging the relevant penalty from the defaulting companies and/or the officers-in-default. Orders of the AO are appealable to the regional director ("**RD**") of the MCA. Non-compliance of such orders (of the AO or the RD) attracts criminal sanctions with penalties. As an effective deterrent, repeated defaults within a period of 3 (three) years from the date of settlement under the IAM Framework could attract a higher penalty.

The entire process is conducted through an online portal and requires physical

attendance only in exceptional circumstances. The IAM Framework is available for offences which attract a penalty of up to INR 2.5 Million (for any offence with the penalty greater than such limit, the relevant forum continues to be the NCLT). These offences include, *inter alia*, issuing of shares at a discount[2], accepting directorship beyond a specified limit[3], and technical defaults/non-compliances relating to form filings with the RoC[4] or sending notices to shareholders (or issuance of proxy) in accordance with the Act[5].

The introduction of the IAM Framework is part of legislative reforms aimed at de-clogging judicial forums such as the NCLT, and reducing their burden by removing minor and technical non-compliances from their jurisdiction. From a litigant's perspective, the IAM Framework provides a cost and time efficient solution for procedural or technical non-compliances, as opposed to the traditional adjudication process before a judicial forum.

THE COMPANIES (AMENDMENT) BILL, 2020

1. Brief legislative background of CAB 2020

CAB 2020 has its genesis in the recommendations made by a committee headed by Mr. Injeti Srinivas (Secretary, MCA) under the Company Law Committee Report published on November 18, 2019 (the "**Law Committee Report**"). In respect of decriminalization of the Act, the Law Committee Report's mandate was limited to compoundable offences[6] and excluded offences related to serious fraud, public interest, and non-compoundable offences. Therefore, CAB 2020 focuses on prescribing an amended framework in respect of the penalties attached to such compoundable offences under the Act.

2. The basis for decriminalization and consequent amendments proposed under CAB 2020

The principle underlying the amendments proposed by CAB 2020 is essentially a test of objective determination versus subjective assessment. In other words, in

[2] Section 53(3) of the Act

[3] Section 165(6) of the Act

[4] Section 86(1) of the Act (Contravention of the provision of dealing with duty to register charges, to report their satisfaction within prescribed timelines and the duty to maintain register of charges); Section 89(7) of the Act (Filing of returns with the RoC within the prescribed time after receiving a declaration of acquisition of beneficial interest in shares from a person)

[5] Section 105(5) of the Act

[6] Compoundable offences are those offences where the prescribed punishment is only fine, or imprisonment or fine, or both. The Act allows for compounding of all offences to which monetary penalty is attached

cases of civil wrongs, i.e., an offence arising from procedural errors or technical lapses, the determination of default is objective in nature, is devoid of any element of fraud or conflict with public interest, and therefore does not merit prolonged adjudication. The Law Committee Report noted that in case of civil wrongs, the wrongful action is bereft of any intention to cause harm, i.e., *mens rea,* which is the predominant element in a criminal action. On the basis of the foregoing principle, CAB 2020 has proposed that offences which relate to violation of a well enunciated legal principle that can be assessed by a *prima facie* objective evaluation be recategorized as civil offences (rather than being criminal actions) under the Act and default thereof be rectified by payment of a prescribed penalty.

The amendments proposed by CAB 2020 to the Act in respect of decriminalization of compoundable offences can be placed into 3 (three) broad categories: (**a**) deletion of a charging provision imposing criminal penalty; (**b**) removal of punishment of imprisonment prescribed for an offence and its recategorization as a civil wrong punishable only with a fine; and (**c**) rationalization of the amount of fines currently prescribed under the Act.

a. Omission of criminal offences from the Act

The Law Committee Report, highlighted the challenges created by multiplicity of laws in India and suggested that where an offence under the Act is also dealt under another specialized legislation such offence may altogether be omitted from the Act. The Law Committee Report recommended the removal of defaults which fall within NCLT's purview and could be resolved by the NCLT's appellate or contempt jurisdiction.

Accordingly, CAB 2020 has proposed omission of 9 (nine) offences which relate to non-compliance with orders of the NCLT, i.e., matters relating to winding-up of companies[7], default in publication of NCLT order relating to reduction of share capital[8], rectification of registers of security holders[9], variation of rights of shareholders[10] and payment of interest and redemption of debentures[11]. Further, in relation to default by the company liquidator in matters relating to conduct of liquidation proceedings[12], CAB 2020 has proposed that such non-compliance of the Act be resolved in accordance with the Insolvency and Bankruptcy Code,

[7] Sections 284(2), 302(4), 342(6), 348(6), and 356(2) of the Act

[8] Section 66(11) of the Act

[9] Section 59(5) of the Act

[10] Section 48(5) of the Act

[11] Section 71(11) of the Act

[12] Section 348(6) of the Act

2016 ("**IBC**"). This amendment is aimed at consolidating the procedural matters relating to liquidation of companies under the IBC which has emerged as a comprehensive code in the matters of winding-up and liquidation.

b. Omission of imprisonment and recategorization of offences

CAB 2020 proposes to omit the punishment of imprisonment in relation to 23 (twenty three) compoundable offences. The nature of monetary levy in each of these offences has been changed from a criminal 'fine' to a civil 'penalty'.

Keeping in view the gravity of offences, a commensurate increase in the amount of penalty has been proposed for 3 (three) offences where the punishment of imprisonment is proposed to be omitted. These offences relate to non-compliances with provisions relating to contribution towards the corporate social responsibility ("**CSR**") fund[13], related party transactions[14], and defaults in submission of material data or statistics to the central government[15].

These amendments are in furtherance of the objective of CAB 2020 to eliminate subjectivity in the adjudication process – which exists in such cases because the Act provides the adjudicating officer with the power to order either a punishment of imprisonment or impose a criminal fine, or both. Furthermore, the Act does not fix the sum of penalty upfront; instead the adjudicating officer has the discretion to choose from a monetary range (minimum – maximum) prescribed under the Act.

Additionally, in an important move to reduce criminal actions arising from procedural non-compliances, 5 (five) offences which relate to delay in filing with the RoC or where default is discoverable by way of reviewing the company's record or the MCA's centralized online repository, have also been proposed to be moved to a system of monetary civil penalty only.[16]

c. Rationalization of amount of fines

CAB 2020 proposes to reduce the quantum of monetary penalty associated with 22 (twenty two) offences. The nature of the monetary levy in each of these cases is also proposed to be changed from a criminal 'fine' to a civil 'penalty'. This category of amendment is aimed at matters relating to maintenance of

[13] Section 135(7) of the Act

[14] Section 188(5)(i) of the Act

[15] Section 405(4) of the Act

[16] Sections 86(1), 89(5), 90(10), 167 (2), and 184(4) of the Act

records by the companies such as, *inter alia*, failure to notify the RoC of alteration of share capital[17], non-compliance with the procedural requirements for transfer of securities[18], failure to maintain registers of members, debenture-holders and other security holders[19], non-compliance in filing of annual return[20], failure in filing certain resolutions and agreements with the RoC[21], etc.

3. Decriminalization under key provisions of the Act

Set out below is a brief overview of the amendments proposed by CAB 2020 to penalties currently prescribed for defaults/non-compliances in relation to the following matters under the Act:

a. Public offer and offer document

CAB 2020 proposes to omit the punishment of imprisonment prescribed under Sections 26(9) and 40(5) of the Act in relation to contravention of provisions relating to public offering of securities by a company, which include, *inter alia*, matters to be stated in the prospectus and separate treatment of application money received pursuant to a public offer. However, the quantum of the monetary penalty under each of these provisions remains unchanged.

Note that the amendment proposed under CAB 2020 in this area will not dilute the risk of non-compliance in respect of the above-mentioned matters in so far as they can be treated as fraud under the Act. In addition, the penalties prescribed under the rules and regulations framed by the Securities and Exchange Board of India ("**SEBI**") for any non-compliance with the above-mentioned matters, may also get attracted.

b. Buy-back of securities

CAB 2020 proposes to omit the punishment of imprisonment prescribed in Section 68(11) of the Act for non-compliance with procedure for buy-back prescribed under Section 68 of the Act, the rules framed thereunder and the SEBI (Buy-Back of Securities) Regulations, 2018. Both the defaulting company and the officer-in-default continue to remain liable for a monetary penalty between INR 100,000 to INR 300,000 for any non-compliance in respect of the manner of conducting a buy-back.

[17] Section 64(2) of the Act

[18] Section 56(6) of the Act

[19] Section 88(5) of the Act

[20] Section 92(5) of the Act

[21] Section 117(2) of the Act

c. Significant beneficial owners

Section 90(10) of the Act provides for imprisonment as the punishment for a significant beneficial owner(s) of an Indian company (a "**SBO**"), who fails to make a timely disclosure of his interests to the company. CAB 2020 proposes not only to omit the punishment of imprisonment for such SBO, but also rationalize the quantum of monetary penalty. While the existing initial penalty of INR 10 Million is proposed to be substantially reduced to INR 50,000, the penalty for each day when the default continues is proposed to be reduced from INR 10,000 to INR 1,000 (subject to a maximum of INR 200,000).

Under Section 90(4) of the Act, the Companies are also required to file the details received from their SBO with the RoC, and failure to do so within the stipulated timeline could attract penalty extending up to INR 5 Million for both the company and the officer-in-default[22]. CAB 2020 has proposed the reduction of the quantum in this penalty such that: (i) the penalty for the defaulting company is capped at INR 100,000 and INR 500 (subject to a maximum of INR 500,000) for each day when the default continues; and (ii) the penalty for the officer-in-default is capped at INR 250,000 and INR 200 (subject to a maximum of INR 100,000) for each day when the default continues.

The above-mentioned proposed amendments indicate that CAB 2020 has distinguished between the liability of a company and its officers, and duly recognized that the financial liability of an officer-in-default should be less than that of the company.

d. Financial statements of companies

CAB 2020 proposes to omit the punishment of imprisonment prescribed in Section 134(8) of the Act for contravention of the provisions relating to preparing and approving financial statements, the auditor's report and the board report. Further, the monetary penalty under this provision has been proposed to be reduced from INR 2.5 Million to INR 300,000 for defaulting companies, and from INR 500,000 to INR 50,000 for the officer-in-default, i.e., almost 1/10th of the existing penalty.

Furthermore, the penalty in Section 137(3) of the Act for a delay in filing the financial statement with the RoC has been proposed for rationalization. The penalty for defaulting companies is proposed to be reduced from a maximum of INR 10 Million to INR 200,000 and from a maximum of INR 600,000 to INR 60,000 for the officer-in-default.

[22] Section 90(11) of the Act

e. Corporate social responsibility

Section 21 of the CAA 2019 had proposed a punishment of imprisonment for a period up to 3 (three) years if a company fails to meet its obligations under Section 135(5) of the Act to make the minimum CSR contribution or transfer its unspent CSR account or a fund approved under Schedule VII of the Act (a "**CSR Fund**"). CAB 2020 has proposed to omit such punishment of imprisonment.

However, CAB 2020 has proposed to replace the fixed monetary penalty with an ad-valorem penalty, the quantum of which is connected to the company's minimum CSR spend obligations. Therefore, a company's risk liability in this matter may either increase or decrease depending upon its profitability in a particular financial year.

CAB 2020 has proposed that: (i) in case of defaulting companies, the maximum penalty should be either twice the amount required to be transferred by the company to the CSR Fund, or INR 10 Million; and (ii) in case of the officers-in-default, the maximum penalty should be one-tenth of the amount required to be transferred by the company to the CSR, or INR 200,000, in each case, which ever is lesser. CAB 2020 has also classified the nature of such fine as civil penalty.

f. Appointment and qualification of directors

CAB 2020 proposes to omit the punishment of imprisonment prescribed under Section 167(2) of the Act in respect of a director who continues to hold office despite being disqualified from it and the office being declared vacant. While the Act allowed for the monetary penalty to be as low as INR 100,000, CAB 2020 has proposed to fix the penalty at the higher amount of INR 500,000.

CAB 2020 has also proposed to reduce the quantum of per day penalty from INR 5,000[23] to INR 2,000 if there is a default committed by a person in holding more than the maximum permissible directorships in companies in India (i.e., 20) in accordance with Section 165(1) of the Act.

g. Related party transactions

CAB 2020 proposes to omit the punishment of imprisonment extending to a period of 1 (one) year, in the event a listed company enters into a related party transaction in contravention of Section 188 of the Act. The Act did not prescribe the punishment of imprisonment in case of such contravention by unlisted companies.

[23] Section 165(6) of the Act

However, given the sensitivity of the offence, the quantum of the fine in case of listed companies is proposed to be increased five-fold i.e., from INR 500,000 to INR 2.5 Million. In case of unlisted companies, the lower range of penalty, i.e., INR 25,000, has been removed and the penalty has been proposed to be fixed at INR 500,000.

h. Oppression and mismanagement

CAB 2020 proposes to omit the punishment of imprisonment for a period of up to 6 (six) months currently prescribed under Sections 242(8) and 243(2) of the Act for matters relating to: (i) amendment of its constitutive documents by a company in contravention of an order of the NCLT; and (ii) a director or officer-in-charge who continues to hold office in a company in contravention of an order of the NCLT, respectively.

However, in each of the above cases, the monetary penalty for the officer-in-default is proposed to be fixed at INR 100,000 (thereby eliminating the lower threshold of INR 25,000), and INR 500,000, respectively. The penalty for defaulting companies remains unaltered.

CONCLUSION

Undoubtedly, the changes proposed by CAB 2020 have the potential of conferring long term benefits on stakeholders and investors by facilitating ease of doing business and providing a swifter redressal and enforcement mechanism for corporate non-compliances in India. In addition, decriminalization of offences under the Act is likely to yield intangible benefits in form of protection of goodwill of a company that could otherwise get tarnished by criminal sanctions being imposed for minor, technical or inadvertent lapses. As the Law Committee Report aptly observed, while criminal sanctions are more grievous and permanent in nature, the cost of civil penalties maybe absorbed as part of running a business in the ordinary course.

However, the legislators should not lose sight of the fact that decriminalization of certain offences under the Act could turn it into a toothless tiger which may fail to seek adequate and necessary compliance by the companies even in relation to matters of grave importance.

Another concern which is worth deliberating upon is if the decriminalization proposed by CAB 2020 will have the effect of encouraging an unbridled corporate culture of purging defaults by merely expending funds, thereby defeating the legislative intent with which CAB 2020 was introduced.

An example of the dichotomy being created by CAB 2020 can be seen in the matter of the burden of compliance that is currently placed upon directors, key managerial

personnel and officers of the company under the Act and the consequences that such officer(s) may have to deal with (in their personal capacity) if their obligations are not discharged in the form and substance envisaged by the Act. CAB 2020 has proposed to reduce the penalty which can be imposed by the Act upon the officer-in-default of the company in various instances. Assuming that CAB 2020 is notified in its current form, the relaxations could potentially encourage executive officers to take an active part and bring their expertise in day to day operational matters of companies without bearing the risk of being exposed to criminal prosecution for actions taken in good faith. At the same time, decriminalization of offences and rationalization of their personal pecuniary liability could also result in officers-in-charge to, henceforth, take a complacent view and a less vigilant approach in maintaining compliances of the company.

It is peculiar that CAB 2020 has been proposed less than a year after CAA 2019 was notified. Both these legislations are propelled by similar objectives and seek to amend overlapping matters. The short time period which has elapsed between enactment of CAA 2019 and introduction of CAB 2020 seems inadequate for the effects (either intended or inadvertent) of legislative changes to corporate laws to percolate down the line to the intended beneficiaries i.e., the corporate entities. While it would take some time for companies to reap the benefits of the amendments relating to decriminalization of offences and recategorization of penalties proposed under CAB 2020, the balance which is critical to attain the overall objectives of the Act itself, must not be lost.

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