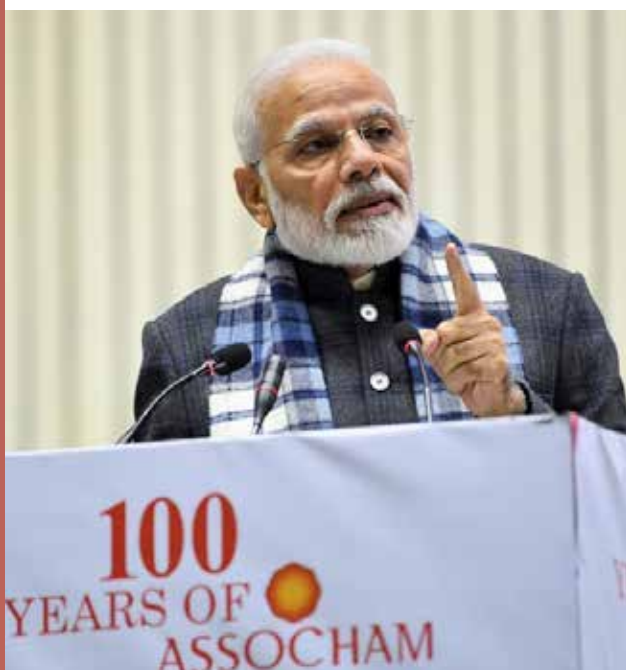




Boost to Ease of Doing Business and Investment in the country

Decriminalization of
offences under the
Companies Act, 2013





“Today, India is undergoing a rapid change in mindsets as well as markets. It has embarked on a journey of deregulation and decriminalization of various offences under the Companies Act. There were hundreds of such provisions in the Companies Act, which allowed criminal action even for small mistakes. Our government has now decriminalized many of these provisions.”

- Prime Minister, Shri Narendra Modi



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Introduction

In case of corporate laws, associating criminality with violation of provisions of law may result in a disproportionately severe penalty for minor misdemeanours. This can have unintended consequences by becoming a significant deterrence for budding entrepreneurs in setting up businesses in the organized sector by incorporating companies, due to the threat of prosecution on account of even minor technical or procedural lapses.

Prior to 2018, the Companies Act, 2013 used to view almost all the violations under its ambit under the lens of criminal law. This led to overburdening of courts with criminal cases and adversely impacted ease of doing business.

Therefore, the government decided to introduce civil liabilities involving in-house adjudication, for dealing with simple defaults which do not involve any fraud or where the nature of the lapse is purely procedural. In doing so, the government has sought to demonstrate its seriousness about promoting ease of doing business for domestic and global investors, along with reducing stress on the criminal justice system and allowing it to focus on grave offences.

Furthermore, a trust-based approach towards compliance builds faith of entrepreneurs in corporate institutions and motivates them to adopt fairer and more transparent business practices.

REFORM – NATURE AND MANNER OF IMPLEMENTATION

1.1 Over the years, for violations under the Companies Act, 2013 the government had been filing criminal cases as per the provisions of the Act. Out of more than 40,000 cases filed under the Companies Act, 1956 and Companies Act, 2013, almost 39,000 cases (more than 97 per cent) did not involve lapses of serious nature.

1.2 This meant that criminal courts were being needlessly burdened with minor cases on account of procedural defaults. Consequently, the courts were not able to pay adequate attention to serious cases of fraud, deceit or injury to public interest.

1.3 The fear of criminal penalty for minor defaults deterred many entrepreneurs. This also impacted the ease of doing business environment in country.

1.4 Therefore, the government decided to undertake a comprehensive review of all the penal provisions under the Companies Act, 2013 so as to identify the nature of each and every default, and ensure that the penal consequences

of any lapse are proportionate to the magnitude of that lapse.

1.5 This exercise was carried out in two phases. Detailed analysis was carried out to calibrate defaults committed by companies and its officers into two broad buckets:

- (1) Defaults which are procedural or technical in nature and,
- (2) Defaults which are serious in nature and may involve larger public interest.

While carrying out this exercise, the government continuously interacted with a cross-section of stakeholders so as to maximize the ease of doing business for honest and law abiding corporates.

1.6 As a result of the comprehensive review, two types of reforms regarding decriminalization of the Companies Act, 2013 were identified. First, changing the nature of certain criminal offences into civil wrongs and second, omitting certain other redundant offences altogether. In addition, alternative means, including through the use of Data Analytics and Artificial Intelligence (AI), were to be leveraged to reduce the very likelihood of the occurrence of defaults.

1.7 The following chart shows the progress of the decriminalization measures through the two amendments of the Companies Act.

Snapshot on decriminalization of offences under the Companies Act, 2013

| | Pre-decriminalization | Post-decriminalization [in two phases] |
|--|-----------------------|---|
| Total penal provisions | 134 | 124 |
| Compoundable offences [mostly fines are imposed] | 81 | 31 |
| Non-compoundable offences [serious offences where imprisonment is ordered upon conviction] | 35 | 35 |
| Defaults subject to civil liability (through In House Adjudication Mechanism) | 18 | 58 |

Benefits of the reform

2.1 Due to decriminalization of minor procedural and technical defaults, the number of prosecutions being filed in the special courts have already started reducing significantly as evidenced by the growing number of defaults being handled through the In-House Adjudication Mechanism (IAM).



2.2 As per data collected from the Registrars of Companies, more than 1400 company law default cases have already been disposed of by the Adjudicating Officers (Registrars of Companies) during the last four financial years (2018-19 to 2021-22) in a summary manner.

2.3 Companies Fresh Start Scheme (CFSS), 2020 was simultaneously rolled out that allowed companies to correct any old defaults related to filing of documents without levy of any additional fees.



- Post reform, more than 1400 default cases decided without resorting to court cases
- More than 4,00,000 companies used Companies Fresh Start Scheme to rectify filing defaults and avoid penalties under Companies Act.

2.4 More than four lakh companies made use of this scheme. They benefited greatly by avoiding heavy additional fees, that they would have been liable to pay otherwise. This one-time measure helped to build an atmosphere of trust.

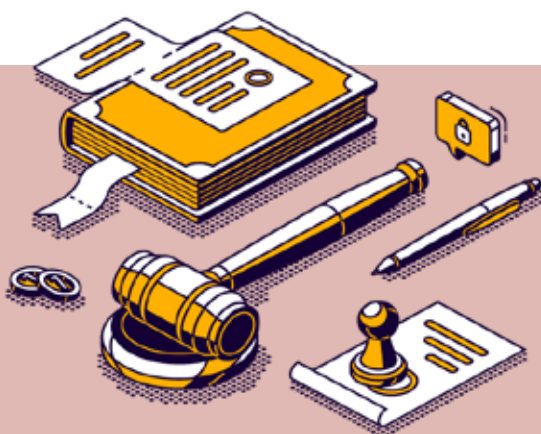
2.5 If the exercise of decriminalization and strengthening of IAM under the Companies Act, 2013 had not been undertaken during 2018-2020, all these cases would have been filed for prosecution before criminal

courts. As a result of these complementary initiatives by the Government of India, the criminal courts can focus on more serious offences.

2.6 Decriminalization has also simultaneously de-burdened the various benches of the National Company Law Tribunal (NCLT), as upon decriminalisation, the companies and its officers would not be required to file applications of compounding before NCLT/Regional Director, so as to escape criminal prosecution.

2.7 The benefits from this reform are many and far-reaching. Apart from freeing up the criminal courts, this reform has also sent out a clear message to the law-abiding corporates at large, about the government's commitment to promote ease of doing business in India around trust.

2.8 These measures would further incentivise



companies to ensure better compliance to our laws while also promoting better corporate management practices in their operations.

2.9 Taken together in the long run, these efforts would encourage budding entrepreneurs to incorporate more companies. Such formal schemes will enable better access to finance & other resources, to build identity & productivity for their business and to grow in a sustainable manner.

2.10 The fruits of the reforms are already evident and more than 1,67,000 companies were registered in India in the financial year 2021-22 which is almost 3 times more than the average number of companies registered annually, six years ago.





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