

# THE POWER OF BEING UNDERSTOOD

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## **Companies Act 2013**

### **- Summary Note on Borrowings by Private Companies**

The Government of India on 1 April 2014 notified various Sections of the Companies Act, 2013 setting out a cumbersome process for making of borrowings by Companies including Private Limited Companies. However, with the Companies (Amendment) Act, 2015 and the notification dated 5 June 2015 issued by the Ministry of Corporate Affairs (MCA) granting exemptions to private limited companies, it is now easier to borrow funds from directors, shareholders, subsidiaries, etc.

Various provisions like obtaining members approval for borrowings above a certain limit, Restrictions on loans to Directors with respect to private companies and applicability of provisions related to Deposits have been made exempt, wholly or in part, subject to certain conditions, which will make way for easier obtaining of loans as far the procedures under the Companies Act is concerned. Furthermore, clarifications have been issued by the Institute of Company Secretaries of India (ICSI) to shed more light on the said subject.

The objective of this summary note is to give an indicative list of persons / entities whom a private limited company generally approaches to raise funds by way of borrowings and the terms and restrictions on making such borrowings as prescribed under the Companies Act, 2013. That apart, a list of entities which may lend funds to companies without it being termed as 'deposits' is being set out.

- 1.1 Borrowings for a Private Limited Company are governed by the provisions of Section 73, 179, and 185 of the Companies Act, 2013 and the Companies (Acceptance of Deposit) Rules, 2014.
- 1.2 In order to borrow monies, the Board of Directors of a Private Limited Company is required to pass a resolution under section 179(3) of the Companies Act, 2013.
- 1.3 The table below outlines the entities or persons from whom a Private Limited Company may borrow funds.

Sr. No.	Entity/ Person	Allowability of the Loan	
1.	Director	<b>Allowed</b> , provided a declaration is furnished by the director that the amount has not been given out of funds acquired by him by borrowing or accepting loans or deposits from others.	
2.	Shareholder	<b>Where money accepted from members <u>exceeds</u> 100% of the Paid up share capital and free reserves.</b>	<b>Where money accepted from members <u>does not exceed</u> 100% of the Paid up share capital and free reserves.</b>
		<b>Not allowed</b>	<b>Allowed</b> subject to: <ul style="list-style-type: none"> <li>■ Passing a members resolution,</li> <li>■ Making provision for security, <b>if any</b> for due repayment of the amount of deposit accepted and interest thereon (not less than 12.5% at present) including creation of charge (Form CHG1) on the property or assets of the Company.</li> <li>■ Filing the details of the money accepted with the registrar.</li> </ul>
3.	Director & Shareholder	<b>Allowed</b> , provided a declaration is furnished by the director that the amount has not been given out of funds acquired by him by borrowing or accepting loans or deposits from others.	
4.	Subsidiary/ Any other Company	<b>Allowed.</b> Not allowed if <ul style="list-style-type: none"> <li>■ Any director of the lending company is a director or member of the borrowing company;</li> <li>■ The director of the lending company, individually or along with one or more of its directors, exercises or controls not less than 25% of voting rights of the borrowing company; or</li> </ul>	

Sr. No.	Entity/ Person	Allowability of the Loan
		<ul style="list-style-type: none"> <li>■ The Board of Directors, MD or Manager of the borrowing Company is accustomed to act in accordance with the directions or instructions of the Board, or any director or directors of the lending company.</li> </ul> <p>However, if the lending and borrowing company are both private limited companies then it can give loan irrespective of common directors if:</p> <ul style="list-style-type: none"> <li>■ In the lending company's capital no other body corporate (body corporate includes a company incorporated outside India) has invested any money i.e., it's shareholder does not include any body corporate;</li> <li>■ If the borrowings of the lending company from banks or financial institutions or anybody corporate is less than twice its paid up capital or Rs. 50 crores, whichever is lower; and</li> <li>■ Lending company is not in default in repayment of such borrowings subsisting at the time of giving such loan.</li> </ul>
	<b>Wholly Owned Subsidiary (WOS)</b>	<b>Allowed</b>
<b>6.</b>	<b>Relative of:</b> <ul style="list-style-type: none"> <li>■ director</li> <li>■ shareholder</li> <li>■ director &amp; Shareholder</li> </ul>	<b>Not allowed</b>
<b>7.</b>	<b>Employee</b>	<b>Allowed</b> The Amount borrowed must not exceed the employees' annual salary in the nature of interest free security deposit.

1.4 Where acceptance of loan from an entity or person is not allowed, such a borrowing may take place nevertheless, subject to the fulfillment of conditions as prescribed in Section 73 of the Companies Act, 2013.

1.5 In addition to the above, a private company can accept amounts of loans from following

- a. Central Government, State Government, Local Authority, Statutory Authority
- b. Foreign Government, foreign or international banks, multilateral financial institutions (Asian Development Bank, International Finance Corporation, etc.), foreign export credit agencies, foreign collaborators, foreign bodies corporate and foreign citizens, foreign authorities or persons resident outside India subject to the provisions of Foreign Exchange Management Act, 1999.
- c. Loan or facility from banking Company, SBI, its subsidiaries, etc. notified by CG as per RBI Act
- d. Loan or financial assistance from Public Financial Institutions, Regional Financial Institutions, Insurance Companies or Scheduled Banks
- e. Amount received against Commercial Papers or other instruments as notified by RBI
- f. Interest free amount received in Trust
- g. Amount brought in by promoters as unsecured loans in stipulation of any lending Financial Institution or Banks subject to:
  - Loan is brought in pursuance of stipulation imposed by lending institutions on promoters to contribute such finance;
  - Loan is provided by the promoters themselves and/or by their relatives.
  - Such an exemption is available only till loans of Bank or FIs are repaid.

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This publication is general in nature. This publication summarises the list of persons / entities from whom private limited companies can accept loans to raise funds by way of borrowings and the terms and restrictions on making such borrowings as prescribed under the Companies Act, 2013. It may be noted that nothing contained in this newsflash should be regarded as our opinion and facts of each case will need to be analyzed to ascertain applicability or otherwise of the respective circulars and notifications and appropriate professional advice should be sought for applicability of legal provisions based on specific facts. We are not responsible for any liability arising from any statements or errors contained in this publication.

4 February 2016

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