

Amendments to Deposit Rules: Reviving Start-Up Ecosystem in India

The Ministry of Corporate Affairs (“MCA”) has amended certain provisions of the Companies (Acceptance of Deposits) Rules, 2014 (“Rules”), vide a notification dated September 7, 2020 (“Amended Rules”). The Amended Rules deal with exceptions to amounts that are considered as a ‘deposit’ for a start-up, under the Companies Act, 2013 (“Act”) and the Rules. The Amended Rules have also aligned the definition of a start-up with the notification dated February 19, 2019, issued by Department of Promotion of Industry and Internal Trade (“DPIIT Notification”) for regulating start-up companies in India.

What is a ‘deposit’?

The provisions relating to acceptance of deposits are governed under Sections 73 to 76A of the Act along with the Rules. Under the Act, a ‘deposit’ is defined to include any receipt of money by way of deposit or loan or in any other form by a company, but excludes, inter alia, (i) loan obtained from a bank, (ii) any amount received from any other company etc. Barring the exclusions as provided under the Rules, any other receipt of money by a company will be deemed as a ‘deposit’ and any acceptance or renewal of deposits in contravention with the Act and the Rules is prohibited.

Deposits can be accepted from public or from members of a company, through the procedure prescribed under the Act read with the Rules. Such acceptance of deposits should be disclosed in the financial statements of the company and

recorded through filing appropriate forms with the Registrar of Companies. Any contravention of the procedure under the Act or Rules with respect to acceptance of deposits, or any failure of the company in repaying the deposit, will attract penalty. The amount of penalty to be paid can be the entire amount of the deposit accepted with interest, along with a penalty which may extend to INR 10 crores.

Amended Rules and its impact

The Amended Rules provides as follows:

- (i) Rule 2 (1) (c) (xvii) of the Rules excludes from the ambit of a deposit, an amount of INR 25 lakhs or more received by a start-up company as a convertible note, not exceeding 5 years from the date of issue in a single tranche, from a person. The Amended Rules have increased the time to 10 years, as opposed to the earlier period of 5 years.

The extended term of repayment gives greater flexibility to start-up companies to raise or infuse capital, which is INR 25 lakhs or more, without it being termed as a deposit.

- (ii) In the explanation to Rule 2 (1) (c) (xvii), which defines a start-up company, an addition has been made to indicate that a start-up company shall mean a private company incorporated in India, in



accordance with the DPIIT Notification.

Earlier, the rules merely defined a start-up as a private company which is incorporated under the Act. However, the DPIIT Notification specifies that an entity shall be considered a start-up, up to a period of 10 years from its date of incorporation and if the turnover of the entity has not exceeded INR 100 crores. This clarification brought in by the Amended Rules aligns the definition of a start-up company under the Rules with that of the DPIIT Notification.

- (iii) Under Rule 3 (3) of the Rules, a private company which is a start-up, can now accept deposits from its members without any limit, for a period of 10 years. Prior to the amendment, the period was 5 years.

Conclusion

The Amended Rules pave way for start-ups to raise money without the fear of the funds being treated as a deposit. This allows greater flexibility for companies to raise funds without attracting the compliances prescribed under the Rules. Also, with Covid-19 impacting operations of numerous start-ups along with drying up their funds, the Amended Rules will help in reviving the start-up ecosystem in India.

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