INFO BYTE

COMPANIES ACT, 2013

Boon or Bane

The Companies Act, 2013 (CA 2013) is turning to be complete Enigma and perhaps a perfect case study on how a Legislation implementation can go wrong. What astonishes is that this act was not conceptualized in a jiffy but almost it took a decade for implementation. The action's of Ministry of Corporate Affairs are confusing gives an impression that there is no thought process in place at the same time soul searching is required from the various stakeholders as why they were not pro -active earlier. All stakeholders are expressing that the legislation should be based on trust rather than suspicion. It is vital to note that the concern of stakeholders can be categorised into two parts. First are those where there are implementations issues arising from mismatch between Rules and the CA 2013 itself and on the Second part are those which arise out of stringent Compliances to be made.

One of the luminaries in the field of Corporate Law and past president of Institute of Company Secretaries of India (ICSI) has written to the Finance Minister, wherein he has opined that the CA 2013 needs to be scrapped wholly and the Companies Act 1956 restored for the time being till a new well drafted legislation is brought in. Union Commerce Minister Nirmala Seetharaman recently has said that the new government would review the Companies Act and a "major" consultation meeting with all stakeholders has been scheduled for the next Saturday to discuss the Companies Act. The Act posed a lot of difficulties and there are areas, which are affecting the stakeholders. All these will be discussed and necessary actions will be taken," she said.

Expressing concerns over the "prescriptive" nature of CSR norms, industry body Confederation of Indian Industry (CII) has sought changes in the social welfare spending rules for corporates besides seeking clarity on taxation aspect. The CII has also said that CSR rules should be in force only after three years. Among others, certain class of companies are required to shell out at least two per cent of their three "Industry is apprehensive that implementation of this provision (CSR) is bound to throw up challenges because of the rather prescriptive manner in which rules have been drafted. There is huge practical concerns on flexibility within legitimate boundaries, and how the monitoring and interpretation of companies' efforts will take place. Further, the industry grouping said the rules do not provide clarity on the taxation front. The representation has also suggestions on various other aspects of the new law, including mergers and amalgamations, one person company, independent directors and related party transactions.

In absence of any unambiguous clarifications from the Ministry of Corporate Affairs, companies are resorting to different interpretations of the provisions. There is no uniform interpretation of even items of ordinary business such as appointment of Independent Directors. Some of the key issues which require immediate attention are:

1. Clarity is required vis-à-vis transitional provisions. For example, while the Act provides transitional period of one year for the appointment of independent directors, constitution of Audit Committee and Nomination & Remuneration Committees is mandatory with effect from 1 April 2014. And thus the two requirements need to be aligned.
2. Directors of the Nomination and Remuneration Committee are expected to prescribe the criteria for evaluation of all directors; carry out evaluation of every director's performance and recommend the appointment and removal of directors. It is also required to lay down remuneration policies. Provisions such as this could make board's functioning difficult resulting in break-down of trust and too much caution. The Act should lay down specific and objective parameters in this regard.

3. Provisions pertaining to Related Party Transactions indirectly seek to vest power in minority in most of cases which is against the fundamental principle of shareholders' democracy and majority rule. Legislation should balance interests of multiple stakeholders and equity must apply to both big and small shareholders to avoid misuse of the provisions by any class – majority or minority Further, the compliance requirement to obtain prior approval of audit committee for all related party transactions is too onerous and may result in Audit Committees not being able to give due focus to key items. Further, transactions between a holding company and its 100% subsidiary do not compromise interests of any stakeholders. However, it still has to comply with all procedural requirements as transactions with other parties.
4. A careful review of the mandate of the Audit Committee is also required. It is for the auditors to monitor and confirm the effectiveness of the systems, processes and controls to the Audit Committee. A reverse obligation on the Audit Committee is clearly unwarranted. Requiring the Audit Committee to evaluate risk management system is also unreasonable.
5. Corporates should be allowed adequate legroom to comply with the CSR provision in a self-responsible manner. Incidental and supplementary activities even if related to Company's business should be allowed as CSR so long as they fall in the activities specified in schedule VII. Onerous provisions would hold back innovation, defeat legislative intent and shift the focus from 'comply with conscience' to 'tick-box compliance.' Government had in fact assured that it will authorize the Boards to choose the scope of CSR activities as it deems fit – this power has not been given in the Act as of now.
6. Private companies which are neither subsidiaries of listed companies nor have substantial borrowings from banks or financial institutions should be exempted from certain provisions of the Act. Such companies should not be treated at par with other public interest entities.
7. Applicability of the requirement of rotation of auditors for companies other than listed companies is also prescribed under the Act. It is suggested that private companies and public companies which do not have substantial public funding should be exempted from this requirement.
8. In addition to the above, there are several inconsistencies between the Act and Rules and at times within the Act itself.

Conclusion

It is to be all along underscored the need for ensuring that the new law aims at progression and development of business instead of impeding it. Law needs to contemplate and weigh up the interests not just of stakeholders but also take forward the business objects of the corporates. Due to the hurried pace in which the Companies Act, 2013 and the Companies Rules, 2014 were implemented; the industry barely got an opportunity to absorb and understand the provisions or their impact in their entirety. Many new concepts are being introduced in the legislation for the first time, and practices with respect to these need to be allowed to evolve over time. However, the rush to notify the Act has introduced disruptive features making it harder for corporates to ensure compliance. For example, the final set of Rules were released in the last week of March 2014 to be implemented from April 1, 2014. **It is very vital for both the Ministry as well stakeholders to recognize that the CA 2013 is going to stay and on urgent basis concern should be addressed well in time.**

S A R T H I
Bridging the Gap

Mumbai
159/11, Amar Brass Compound,
Vidya Nagari Marg,
Kalina, Santacruz (E),
Mumbai – 400098
Landline: 022-26528671-72
Fax: 022-26528673

New Delhi
Anthem House,
E-360, 1st Floor,
Nirman Vihar, Delhi - 110092
Landline: 011-22449817,
011-22449815
Fax: 011-22439816

CONTACT US
Please write to us with your feedback, suggestion or query at smelisting@sarthiwm.in
www.sarthiwm.in | www.smelisting.net

Sarthi Capital Advisors Pvt Ltd
SEBI Registered Category I Merchant Banker
SEBI Registration No: INM000012011