Phased rollout of new companies act creating confusion

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Phased rollout of new Companies Act leaves India Inc in a tizzy

Govt chose to notify sections which did not require any rules, thinking that these are on a standalone basis

On August 30, when the government notified the new Companies Act, 2013, exactly a day after the Presidential assent -replacing a nearly six-decade legislation that governs companies in the country - it inadvertently left many auditors, legal experts, and finance teams across corporates in a tizzy.

While the government has notified 98 sections of the new Companies Act, 2013, where rules were not required, it has failed to notify various sub-sections linked to the 98 sections, leading to utter confusion.

The Ministry of Corporate Affairs (MCA) tried to address the issue by bringing in two separate clarifications, on September 12 and 18. It was belatedly clarified that the provisions of the old Act corresponding to the notified provisions of the new Act have "ceased to be effective" (in advance of the formal repeal of such provisions), but the problem largely pertains to the overlapping areas between the two legislations.

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"This was bound to happen, as the government chose to notify those sections, which did not require any rules, thinking that these sections are on a standalone basis," says Harinderjit Singh, partner, PricewaterhouseCoopers.

For instance, MCA has several definitions including those for associates, controls and subsidiaries. However, it has not defined joint ventures and not notified sections related to consolidating two financial statements.

Similarly, while the ministry notified Section 185 on loan to directors, a related section - Section 186 on loan to any person - has not been notified.

According to Pavan Kumar Vijay, managing director of financial consultancy firm Corporate Professionals, any law which is not fully notified is legally not implementable.

"The industry has started discussions and consultations on the matter and the ministry should now take proactive measures to address the issue," says Vijay.

The situation of having two legislations in force on the same subject matter is certainly peculiar and creates administrative burden for corporates. For instance, a "subsidiary" is defined differently in the old Act and the new Act. As a result, one may have to refer to the definition of "subsidiary" under the new Act to apply to provisions under the old Act.

Also, while the definition of a "foreign company" has not been made effective under the new Act, the provisions applicable to foreign companies are in effect. In such a situation, it is unclear whether one would need to look at the old Act for the definition of "foreign company" and apply this to the new Act.

At the moment, corporates and their consultants have to be mindful of both legislations, as well as the draft rules published by the MCA to ensure compliance with the law.

However, this could have been avoided by notifying all the provisions of the new Act. "A delayed effective date before the provisions became effective would also have made the transition much easier," says Rajat Sethi, partner, S&R Associates.

Mehul Modi, senior director, Deloitte Touche Tohmatsu India, points out that the 2013 Act requires the financial year (FY) to uniformly end on March 31. Under the 1956 Act, freedom was given to companies to determine the FY.

In the new Act, all the definitions are yet to get notified, so the 1956 Act needs to be followed in those cases. In any case, transition of two years is available to meet the 2013 Act provisions related to FY.

But there are people in favour of the method of rollout. "It will make it easier for companies to absorb the implications o f the notified sections more thoroughly and then get ready for the next notification," says Vijaya Sampath, senior partner, Lakshmi Kumaran & Sridharan.

When the new Companies Act was introduced in the United Kingdom, it was done in phases and it took a long time to implement the entire Act.

The new Act has introduced many new concepts and nuances, too. "This is the first time that the MCA has sought public consultation in such a web-friendly and open manner," points out Sampath.

Timing is also an issue. If the government had waited for all the draft rules to become final and then released the Act and the rules at the same time, it might have been difficult for companies to comprehend the implications.

Phasing the Act, in that sense, is a good way to allow corporates to understand the impact of the notified sections and make necessary changes in the companies.

ICAI President Subodh Agarwal says, "Having both the Acts in place will help faster implementation of the new Act."

MCA officials plan to notify all the rules before the year-end and the Act, in its entirety, will be in place by early next year. However, the full import of the new Act may come into effect from the next financial year (2014-15). Till then, India Inc has to live with some confusion.

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