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The Companies Act 2013: The Coveted Development Tool in Modern Globalised Era

KEYWORDS

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ABSTRACT *The new Companies Act 2013 is being recognised as "Landmark legislation". It has been warmly accepted by the modern era organisations and specially those, who have to implement it. The main aim of this new act, almost a 10 year rigorous exercise, is to change the focus on "raising the bar on governance" and in a elaborated form and intend to deal with relevant themes such as investor protection, fraud mitigation, corporate social responsibility, auditor accountability, reporting framework, director responsibility and efficient restructuring. This is expected to make changes in Indian corporate law in the context of the changing economic, social and business environment. In today's globalised era, this would make Indian corporate environment more transparent, simple and acceptable. The former act being 50 years old was facing hassle in handling challenges of growing industries and the interests of the increasing class of sophisticated stakeholders. The objective of this paper is to highlight the changes, specifically in reporting and auditing practices such as board reports, internal financial control, higher auditor accountability etc. The data for this purpose was collected from secondary resources such as the bare act and other reports. This paper further discusses the practical perspectives of such change in Companies Act with respect to actual implementation.*

INTRODUCTION:-

It is said that to changes is the key to success, even more in the present era of Industrialisation and globalisation, The 1956 Act has been in need of a substantial revamp for quite some time now, to make it more coeval and relevant to corporate, regulators and other stakeholders in India. Hence, after a gap of 57 years the companies act, 1956 has now been replaced by The Companies act 2013, with a more simplified and rationalised legislation. It received the President's assent on 29 August 2013 and has now become the Companies Act, 2013. It contains precisely 470 sections and 7 schedules as compared to 658 sections and 15 schedules in the previous act However, the key highlight of this 2013 Act is also the extent of subordinated legislation. The full impact of the 2013 Act can only be understood when the related Rules get finalized and the two are read together. Aimed at the one objective – 'Raising the Bar on Governance', the act can be further understood in the light of following objectives.

1. Increased Reporting Framework
2. Higher Auditor Accountability
3. Easier Restructuring
4. Wider Director and Management Responsibility
5. Inclusive CSR Agenda
6. Emphasis on Investor Protection Increased Reporting Framework Higher

Changes in Financial Reporting and its Perspectives
Uniform Financial Year

The companies Act 2013 has introduced significant difference in the definition of the term "financial year" Which has been defined in section 2(41) of the act to mean April to March companies which are currently following a different financial year need to align with the new requirement within two years.

There are several changes in board report but the changes which have gathered the attention of users are as follows:

1. Extract of annual report covering following matters

New format of annual return is comprehensive with non-financial information. It should contain information up to the closure of F.Y. and not up to AGM date.

Every return duly signed by director, Company Secretary(CS), or CS in practice. Return to the certified by CS in practice also state that companies has complied are provision of the act for following company.

- Indebtness
- Shareholders pattern
- Details of promoters, directors & Key Managerial Personnel (KMP) and if any changes therein.
- Details of board meeting & attendance
- Remuneration of directors and KMP (salary perquisites, stock option, sweat equity as percentage of profits, other commissions to specify.
- Penalty and punishment imposed on company & its directors/ officers.

2. Composition of CSR committee, CSR policy, its contents and annual report on CSR activities.

3. Disclosure regarding median remuneration.

Section 197 of 2013 act requires every listed company to disclose in its board report the ratio of the remuneration of each director to the median's employee remuneration and other details as required. The managerial personnel rules clarify how it is calculated.

4. Declaration of independent director

First time after appointment of independent director it furnishes a statement to the effect that independent director possess appropriate balance of skill experience and knowledge.

5. Explanation or comments by the board on every qualification, reservation or adverse mark or disclaimer made

a. By the auditor in his report and
b. By the company secretary in practice in his secretarial audit report, Secretarial audit report to be annexed to

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the board report.

6. Particulars of loans, Guarantee or investment.

The 2013 Act states that companies can make investments only through two layers of investment companies subject to exceptions which includes company incorporated outside India [section 186 of 2013 Act]. There are no such restrictions which are currently imposed under the 1956 Act.

Further, the exemption available from the provisions of section 372A of the 1956 Act to private companies as well as loans or investment given or made by a holding company to its subsidiary company are no longer available under the 2013 Act

7. Detailed revision of financial statement: Under the old act companies are generally not permitted to revise or restate financial information presented in their financial statements. Material misstatements in the accounts related to previous years, whether due to occurrence of fraud or error are reported as a 'prior period adjustment' in the financial statements of the year / period in which such misstatements are discovered.

8. Receipt of commission by a director form the holding/ Subsidiary company.

9. Additional information & Director's responsibility statement.

- Statements that the directors had upgraded with the proper system and compliance with provision of all applicable statue and that such system were adequate and operating.
- Internal financial control Section 134(5)(e) of 2013 act states as follows:

"For the purpose of this clause the term 'internal financial control' means the policies and procedures adopted by company for ensuring the orderly and efficient conduct of its business, including adherence to company's policy, the safe guard of its assets, the prevention and detection of fraud and order, the accuracy and completeness of accounting records and timely preparation of reliable financial control."

It laid down wide responsibility of internal financial control reporting on the shoulders of directors, it can be breakdown in two parts.

" Financial reporting control" related to financial reporting aspect.
" Business control" related to strategic and operational aspect of the business.

10. Pre revised clause 49, RC 49

It requires that as a part of the director's report or as an addition there to, a MD & A report should form part of the annual report to the shareholders. This MD&A should include discussion on the following matters, within the limit set by the company.

- Industry structure and development,
- Opportunities and threats,
- Segment or product wise performance,
- Outlook,
- Risk and concerns,
- Internal control systems and there adequacy,
- Discussion on financial performance w.r.t. operational performance.
- Material development in Human Resources/ Industrial relation fromt including number of people employed.

11. Preparation of Board Report

The account rules require that the board report will be prepared based on the SFS (Standalone Financial Statement) of a company. This report must contain a separate section, wherein the performance and financial position of each subsidiary, associate and joint venture company included in the CFS (Consolidated Financial Statement) is presented.

Conclusion:

1. Disclosure under RC49 are similar to those under prerevised 49, but companies need to ensure proper synchronisation of these disclosures with new disclosures under the 2013 act. In case of a listed company the board need to disclose information under the 3 heads viz. Boards report, Director's Responsibility statement & MD&A. It is upon the listed company weather it presents MD&A separately in annual report or as a part of Board report itself. Though information requirement in both report are worded differently from practical perspectives, the presentation of such information is likely to significantly overlap each other. Therefore a listed company needs to structure its Board report and MD&A cautiously so that meaningful information is presented without duplication and ensuring compliance with both the requirements to the user.
2. The disclosure for each subsidiary associated and Joint venture may become very cumbersome for companies. The investors and analysts typically look at the performance and financial position of the consolidated group as against each individual identity, therefore groups will have to provide, standalone performance of each company for complying with 2013 act and consolidated performance for the benefits of investors and stakeholder.
3. The disclosures regarding median remunerations which are in many respects consistent with disclosures required globally. The managerial personnel rules clarify that median means the numerical value separating the higher half of the population from lower half and the median may be found by arranging these observations from lower to higher value or visa-versa and picking the middle one. The comparison of workers remuneration with that of CEO will reflect significant disparity and may not give any useful information to users and secondly the disclosure of employee who are not directors but receiving higher remuneration during the year may bring in to the notice of the real decision maker. Moreover disparity may arise in case of a company which has branches in many countries where remuneration is higher because of inclusion of foreign salaries to Indian workers so to determine the median, it may reflect the distorted comparison.
4. There are various view in respect of "Internal Financial Controls". One view states that director's reporting on financial control only in case of listed companies. In contrast auditor are required to report the existence and operating effectiveness of internal financial control of all companies ,so to bridge this gap, the accounts rules require director of even non-listed companies to comment on the matter. So under this argument there is no conflict between 2013 Act and

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account's rule as the directors' responsibility with regard to reporting on financial control will be in sync with auditors responsibility. In listed companies responsibility it based on wider definition of internal financial control, which includes both financial as well as business control, but in case of non-listed company the definition has narrowed down to financial reporting control.

5. Other view is that the MCA has included this provision in the accounts rules to address the question being raised about the definition of internal financial control and with the aim to be in the same line with regard to global practise. So the intention of MCA has been restricted to listed companies with regard to internal financial control.
6. There are two fall outs, firstly it is trying to narrow the internal financial controls and the accounts rules have unwittingly made requirement applicable for non-listed company. And secondly the accounts rules overriding the 2013 Act.
7. Rotation of auditor will definitely improve the independence but on other hand it also increases the associated cost, imposing excessive burden on companies and increasing the risk that new auditor may not be able to detect errors and fraud and little chances to enhance the audit quality.
8. Sec 141 of the 2013 Act, dealing with eligibility, qualifications and disqualification. Its clause (3)(h) states that a person who has been convicted by a court of an offence involving fraud and a period of 10 years has not been elapsed from the date of conviction is not eligible for appointment as auditor. This section doesn't refer to "order/pending proceedings relating to matters of professional conduct" as a criteria for disqualification.

The wording used in disqualification of auditor it is not clear whether the Rs. 1 Lac/ 5Lac limit applies separately to each relative or collectively to all covered person including auditor and all his relatives and partner. It is also not clear whether the limit will apply separately for the company, its each subsidiary, holding company etc or collectively to all these company.*

Reporting of fraud to central government proves to be challenging if the auditor is required to comment not only on confirmed fraud but also suspected fraud.

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