

Samriddhi, The Prosperity Foundation

Recommendations from Samriddhi Foundation in the new draft Act replacing the Company Act, 2063 (2006)

The ease of doing business as measured by the World Bank Group all over the world points out 'simplified incorporation process' as one of the key features to promoting private entrepreneurs to enter the economy. In Nepal, the registration of a company falls under the jurisdiction of Company Act 2063 (2006). The Government of Nepal has taken a proactive role in identifying issues under the current Company Act, 2063 and reviewing it accordingly. Starting a business regulations and legislations have progressively been eased up by the Government of Nepal over the last two decades.

Nepal stands at 108th rank out of 186 countries in the World Bank 'Doing Business' survey.

This document aims to outline primary areas that require further discussion during the current review and amendment process. Following are some of the key issues that needs to be reviewed under the current Company Act, 2063:

Incorporation process simplification:

It is now a common trend around the world to simplify the process of incorporation in terms of streamlining the processes as well as simplifying the processes involved. The trend is for companies to get registered on the basis of a single document of incorporation with Articles of Association (AoA) being the favored document. The Company Act, 2063 currently provisions several steps as well as documents of incorporation, which could be simplified to a single document to ease up the process further.

Restructuring of Office of the Company Registrar (OCR):

Although the Company Act, 2063 provides executive powers to the OCR, in practice, the OCR has also been taking up the burden of judicial functions including rejecting companies on the basis of the content of documentation provided. This has created confusion and an impenetrable system, which promotes rent seeking avenues and non-transparency. Therefore, the executive powers of the OCR need to be more explicit while the Company Act should, explicitly remove the judicial functions that it practices at the moment.

Similarly, as Government of Nepal has already moved towards a mandatory online registration system, OCR needs to reflect this up-gradation in its structure as well. This requires a review of the kind of human resource required by OCR and the incentive based performance review system that rewards them accordingly. The Company Act needs to address this issue in detail.

The online system should enable any person(s) to incorporate their company from any location in Nepal. Currently the systems is centralized thereby requiring business people from outside the capital having to come to the capital for registration. Therefore, another aspect of restructuring needs to address the kind of decentralization required for enabling a simpler process of acquiring a Certificate of Incorporation. The underlying theme in the restructuring effort should be on making it more investment and business friendly.

Samriddhi, The Prosperity Foundation is an independent policy institute based in Kathmandu that focuses on economic policy reform. Established in 2007, Samriddhi aims at facilitating a discourse on pragmatic market based solutions for a free and prosperous Nepal. Samriddhi is a member of the Economic Freedom Network and is the co-publisher of the Economic Freedom of the World Report with the Fraser Institute, Canada.

Restructuring the Board of Directors:

Progressive developments in Company Act mandate the companies to protect the rights of all kinds of shareholders. This is especially true in case of public limited companies with a diversity of small-scale shareholders. Therefore, the Company Act should address this by mandating a restructuring of Board of Directors to include at least one representative of minority shareholders. This will ensure that the voices of small shareholders are also represented at the Board of Director's level. Similarly, some Company Acts such as that in India have mandated having at least one woman represented in the Board of Directors. Such provision would help make our Company Act more inclusive.

Company structures and conversion:

There are limits to the number of shareholders provided for private limited company by the current company act. This kind of provision should be removed as it has no logical connection to how the company is run. Similarly, the conversion of companies from one form to the other (such as from private to public limited or from profit distributing to profit not distributing) is a cumbersome process filled with uncertainties. This conversion process should be made easier and transparent such that it facilitates the transformation of companies in response to market conditions and enables the economy to function better.

Inter company lending and investment:

Provisions for inter company lending and investment needs to be made easier such that we can create a dynamic secondary capital market. The current provisions have several restrictions that make inter company lending and investment difficult. This prevents the companies from flexibility to adapt to differing market conditions and opportunities.

Exit Procedures:

The exit provisions in the current company act need to be rationalized as well. Currently, the problem does not lie much with solvent companies that want to exit. It is primarily an issue for insolvent companies due to the directive issued by Nepal Rastra Bank listing the owners of such companies in the 'black list'.

Similarly, the current provisions have not really addressed the exit of cross border insolvency including the exit of branches of Multi national corporations.

Rationalization of fines, punishments and appeals:

The current regime of fines, punishments and appeals discourages several entrepreneurs owing to the high cost of compliance. Therefore, these provisions need to be revised. The underlying theme in terms of fines, punishments and appeals should be to encourage more transparency and appropriate recovery measures in case of publicly listed companies and companies using public monies (even those using public monies through financial intermediaries).

Compliance and Certification and Transparency:

In the age of Global standards and practices, it is imperative for Nepali companies to update their practices. This needs to be reflected in Company Act. The burden of certificate of compliance should be passed on to the companies to be issued by the Chairperson and Company Secretary thereby promoting self-governance. Similarly, public documents can be put in the public domain such that any citizen can access it. This would encourage transparent behavior and practices amongst companies. The publication of company documents can be made according to set standards and criteria (for example for companies transacting above a certain volume of transaction or for companies with a certain amount of paid up capital).

1. IT related provisions:

The new Company Act needs to reflect the reality of online registration thereby providing validation to electronic documents uploaded by the companies. This would streamline processes and simplify the registration of businesses. Some of these provisions include:

- “register of companies” means the register of companies maintained by the Registrar on paper or in any electronic mode under this Act
- Maintenance and inspection of documents in electronic form
- Electronic form to be exclusive, alternative or in addition to physical form
- Electronic filling of documents to be exclusive, alternative or in addition to physical filing
- Provision of value added services through electronic form
- Provisions relating to filing of applications, documents, inspection, etc., in electronic form.

Corporate Social Responsibility (CSR):

CSR should be encouraged. Broad areas need to be guided by the Act. (Should be indicative) – especially for profit making company. Incentivize CSR with tax deduction. Corporate Social Reporting Card. CSR can be shown as expensive.

In addition, there are debates surrounding the adequate provisioning for Corporate Social Responsibility (CSR) as well as rewards and/or recognition for companies that are socially and environmentally responsible. Such social provisions also need to be addressed by the amendment to the Company Act in some form or the other.

Avoiding irrational and inconsistent provisions:

The existing Company Act needs to be reviewed for irrational and inconsistent provisions. The amendment should also incorporate the repeal of such provisions from the current Company Act.

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