THE ECONOMIC TIMES
Tue, Sep 07, 2010 | Updated 12.08PM IST

7 SEP, 2010, 05.10AM IST, SHAILESH MENON,ET BUREAU

Cos take the 'easy' way out in liquidation drive

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MUMBAI: The 'easy exit scheme' proposed by the Ministry Of Company Affairs (MCA) has received an overwhelming response from promoters who want to wind up their loss-making ventures without too many regulatory hurdles. According to MCA scrolls, 15,000 companies have hit the road to easy liquidation - about 1,815 of them being finance and investment firms.

Of the firms opting for easy winding up of business, 591 are investment & holding companies, 557 leasing & credit companies, 419 chit funds and 248 securities & financial services companies. As per Companies' Act, a registered company cannot shut shop without approvals from various authorities and the court. The MCA annual report says about 6,300 companies applied for shutting business last fiscal and only 174 got court permission.

"Promoters are making good use of the amnesty scheme. The 'easy exit scheme' cuts a lot of legal tangles which is otherwise prevalent in times of regular winding up," said Arun Bhattar, a Mumbai-based company law advisor.

The Ministry has broadly given permission to promoters (groups or institutions) to down the shutters of their defunct companies provided they have no public debt on their books. The last time MCA came out with a similar scheme was in 2000. The 'easy exit scheme' was open between May 30 and August 31.

According to Mr Bhattar, by opting for easy liquidation, promoters will also save on effort and costs towards annual compliance. Corporate houses having unused investment arms or idle SPVs (special purpose vehicles) have also benefited from the amnesty scheme.

Finance and investment companies account for about 12% of the overall 'easy liquidation pie.' According to corporate lawyers, a good number of these firms are 'shell companies' floated by large corporates to source their investments. The list also includes several 'private finance companies' (chit funds and the like) that have been barred from collecting public deposits. Investment or security broking firms that have gone bust or are finding it difficult to do business are also in the line to shut shop.

"Regular liquidation is a tedious and long-drawn procedure. It may take a couple of years and a series of court sessions before a company could shut shop. Promoters have made good use of the easy exit scheme; it has allowed promoters to wind up their shell companies at lower cost and lesser time," said Siddharth Shah, who heads the corporate & securities practice group at Nishith Desai Associates.

According to Mr Shah, tightening of banking and finance rules, increased transparency and net sworth criteria have resulted in several finance and investment companies closing business. "NBFC registration has become mandatory for private finance companies; transparency is very important now and tax laws have become more stringent. These factors have resulted in several companies opting for liquidation," Mr Shah added.

The closure of such finance companies and 'shell companies' will not have any significant impact on debt or equity market inflows or investments, Mr Shah added.

According to Pranay Bhatia, associate partner at Economic Laws Practice, a multi-layer corporate structure leads to tax leakage in form of dividend distribution tax (DDT). As a result, companies are trying to mitigate this (DDT) cost by moving from corporate structure to Limited Liability Partnership (LLP) structure.

"Promoters could hold their investments in the operating companies through LLPs, which does not have to pay tax on distr butable dividends. This has already led a few promoter groups to move their holding from corporate to LLP structure. This could have also led to closure of a few of the investment companies," Mr Bhatia added.

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