

Chapter - 3

"Appointment and Remuneration of Managerial Personnel"

| | |
|------|--|
| (iv) | <u>Sec. 198: Calculation of profits:</u> |
| | <u>Sec. 198(1):</u> In computing net profits of a company in any FY for Sec. 197: |
| | (a) credit shall be given for the sums specified in Sec. 198(2); |
| | (b) credit shall not be given for those specified in Sec. 198(3); |
| | (c) the sums specified in Sec. 198(4) shall be deducted; and |
| | (d) the sums specified in Sec. 198(5) shall not be deducted. |
| | <u>Sec. 198(2): Items of which Credit is to be given:</u> |
| | Bounties & subsidies received from any Govt. or any public authority. |
| | <u>Sec. 198(3): Items of which Credit shall not be given:</u> |
| | (a) Premium on shares or debentures, issued or sold by the company unless |
| | the company is an investment company; |
| | (b) Profits on sales of forfeited shares; |
| | (c) Profits of a capital nature including profits from sale of any undertaking; |
| | (d) Profits from sale of any immovable property or fixed assets, unless it is |
| | the company's business: |
| | Provided that where sales value exceeds exceed WDV, credit shall be |
| | given for so much of the excess as is not higher than the difference |
| | between the original cost of that fixed asset and its WDV; |
| | (e) Any change in carrying amount of an asset or liability on measurement of |
| | the asset or liability at fair value; |
| | (f) Amount representing unrealised or notional gains or revaluation of assets. |
| | <u>Sec. 198(4): Sums allowed to be deducted:</u> |
| | (a) All the usual working charges; |
| | (b) Directors' remuneration; |

| | |
|------|--|
| (v) | <p><u>Sec. 199: Recoverability of remuneration in certain cases:</u></p> <p>Without prejudice to any liability incurred under the provisions of this Act or any other Law</p> <p style="text-align: center;">↓</p> <p>where a company is required to re-state the F.S.</p> <p style="text-align: center;">↓</p> <p>due to fraud or non-compliance with any requirements of this Act and the rules made thereunder</p> <p style="text-align: center;">↓</p> <p>the company shall recover from any past or present <u>M.D / W.T.D./ Manager</u> or <u>CEO</u> who during the period for which F.S. are required to be restated</p> <p style="text-align: center;">↓</p> <p>received the remuneration in excess of what would have been payable to him as per restated F.S.</p> |
| (vi) | <p><u>C.G. or company to fix limit with regard to remuneration: Sec. 200 and Rule 6</u></p> <p>- A company may, while according its approval u/s 196, to any appointment or to any remuneration u/s 197, fix the remuneration, at such amount or %age of profits, as it may deem fit.</p> <p>- While fixing the remuneration, the company shall have regard to the following:</p> <ul style="list-style-type: none"> (i) financial position of the company; (ii) remuneration/commission drawn by individual concerned in any other capacity; (iii) remuneration or commission drawn by him from any other company; (iv) professional qualifications and experience of the individual concerned; (v) <u>such other matters</u> as may be prescribed (Rule 6). <ul style="list-style-type: none"> • Financial & operating performance of company during 3 preceding FYs. • Relationship between remuneration and performance. • Whether remuneration policy for directors differs from remuneration policy for other employees and if so, an explanation for the difference. • Securities held by the director and details of shares pledged. |

| | |
|-------|--|
| (vii) | <u>Compensation for loss of office of MD/WTD/Manager (Sec. 202):</u> |
| | <u>Sec. 202(1): Compensation to MD etc.</u> |
| | A company may make payment to a MD/WTD/Manager |
| | ↓ |
| | but <u>not to any other director</u> by way of |
| | - compensation for loss of office, or |
| | - as consideration for retirement from office, or |
| | - in connection with such loss or retirement. |
| | <u>Sec. 202(2): Situations in which compensation is not payable:</u> |
| | No payment shall be made u/s 202(1) in the following cases, namely: |
| | (a) where the director resigns as a result of reconstruction and appointed as MD or WTD, Manager or other officer of reconstructed entity. |
| | (b) where the director resigns otherwise than on reconstruction. |
| | (c) where the office of the director is vacated u/s 167(1). |
| | (d) where the company is being wound up, due to negligence of director. |
| | (e) where the director has been guilty of fraud in relation to, or of gross negligence in or gross mismanagement of, the conduct of the affairs of the company or any subsidiary company or holding company thereof. |
| | (f) where the director has instigated or has taken part directly or indirectly in bringing about the termination of his office. |
| | <u>Sec. 202(3): Limit of compensation payable u/s 202(1):</u> |
| | $\text{Compensation payable} = \text{Permissible period} \times \text{Average remuneration}$ (Max. Limit) |
| | Step - 1: Permissible period: Remaining period of service or 3 years - whichever is shorter. |
| | Step - 2: Avg. Remuneration: Average of Actual remuneration earned during: |
| | (a) 3 years immediately preceding the date of cessation of office. |
| | (b) the period, he held the office, if the period of holding office < 3 years. |

| | |
|--|---|
| | <u>Sec. 202(4):</u> Noting in Sec. 202 shall be deemed to prohibit the payment to a MD/WTD/ Manager of any remuneration for services rendered by him to company in any other capacity. |
| | <u>Bell. Vs. Lever Bros:</u> Compensation already paid cannot be recovered subsequently on discovering any breach of duty or corrupt practices on part of the MD/WTD/Manager, to whom compensation was paid. |
| DO Practice - Questions on Sec. 202 | |
| (viii) | <u>Appointment of KMP (Sec. 203):</u> |
| | <u>Sec. 203(1): Companies requiring to appoint KMP:</u> |
| | Every company belonging to such class or classes of companies as may be prescribed (Rule 8 and 8A) shall have the following whole-time KMP: |
| | (i) MD or CEO or Manager and in their absence, a Whole-Time director; |
| | (ii) Company Secretary; and |
| | (iii) Chief Financial Officer. |
| | <u>Rule 8:</u> Every listed company and other public company having PUSC of \geq ₹ 10 Cr. |
| | ↓ |
| | shall have whole-time KMP. |
| | <u>Rule 8A:</u> <u>Appointment of Company Secretaries in companies not covered under Rule 8:</u> |
| | Every <u>private company</u> which has a PUSC of \geq ₹ 10 Cr. |
| | ↓ |
| | shall have a <u>whole-time company secretary</u> . |
| | <u>Provisos to Sec. 203(1): Prohibition on individual to be appointed in multiple positions:</u> |
| | <u>1st Proviso:</u> An individual shall not be appointed or reappointed as chairperson of company as well as the MD or CEO of the company at the same time unless, |
| | (a) the articles of such a company provide otherwise; |
| | or |
| | (b) the company does not carry multiple businesses. |

2nd Proviso: Nothing contained in 1st proviso shall apply to prescribed companies engaged in multiple businesses and which has appointed one or more CEOs for each such business as may be notified by the C.G.

Companies Notified for purpose of 2nd proviso to Sec. 203(1):

- Public companies having Paid up share capital* of \geq ₹ 100 crore and annual turnover* of \geq ₹ 1,000 crore which are engaged in multiple businesses and have appointed CEO for each such business.

*on the basis of the latest audited balance sheet.

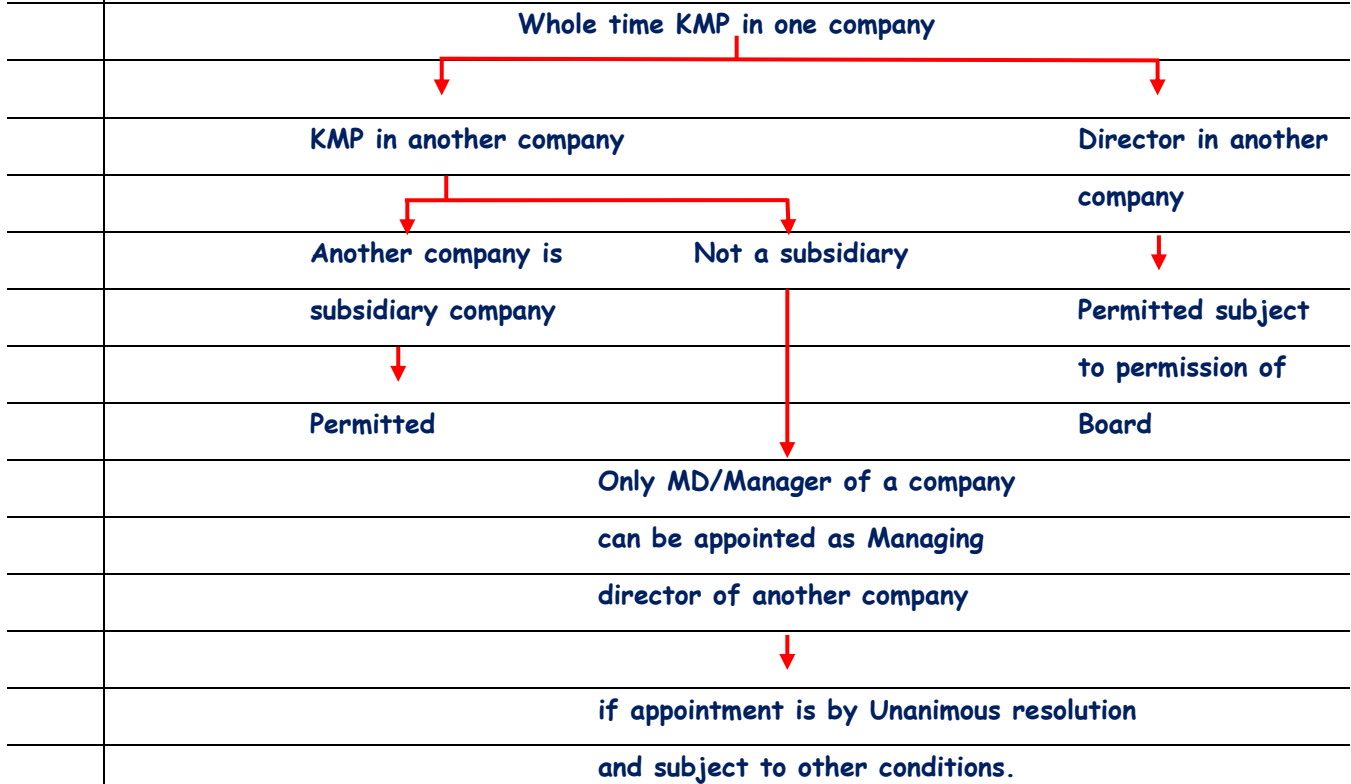
Example on Sec. 203(1):

| Name of Co. | Nature of Co. | PUC | Rule 8 applicability | Rule 8A (applicability) |
|-------------|---------------|--------|----------------------|-------------------------|
| A Ltd. | Listed | 4 Cr. | Yes | N.A. |
| B Ltd. | Listed | 12 Cr. | Yes | N.A. |
| C Ltd. | Unlisted | 4 Cr. | No | N.A. |
| D Ltd. | Unlisted | 12 Cr. | Yes | N.A. |
| H(P) Ltd. | Unlisted | 4 Cr. | No | No |
| I(P) Ltd. | Unlisted | 6 Cr. | No | No |
| J(P) Ltd. | Unlisted | 12 Cr. | No | YES |

Sec. 203(2): Conditions for appointment:

Every whole time KMP shall be appointed by means of a Board Resolution containing the terms and conditions of appointment including remuneration.

Sec. 203(3): Restrictions on number of companies:



Examples on Sec. 203(3):

| | Existing Position | Proposed Appointment | Remarks |
|-------|--|------------------------------------|---------------------------------------|
| (i) | KMP in H Ltd. | KMP in S Ltd. | Permitted |
| (ii) | KMP in A Ltd. (Other than MD/Manager) | KMP in B Ltd. | Not permitted |
| (iii) | KMP in A Ltd. (MD/Manager) | KMP in B Ltd. (other than M.D.) | Not permitted |
| (iv) | KMP in A Ltd. (MD/Manager) | KMP in B Ltd. (M.D.) | Permitted subject to conditions |
| (v) | KMP in A Ltd. | Director in B Ltd. | Permitted subject to Board permission |
| (vi) | MD in A Ltd. and B Ltd. | M.D. in C Ltd. | Not permitted. |

| | |
|--|---|
| | <u>Sec. 203(4): Filling of Casual Vacancy:</u> |
| | If the office of any whole-time KMP is vacated, the resulting vacancy shall be filled-up by the Board at a meeting of the Board within a period of <u>6 months</u> from the date of such vacancy. |
| | <u>Sec. 203(4A): Exemption to Govt. Company:</u> |
| | The provisions of Sec. 203 shall not apply to a MD or CEO or Manager and in their absence, a WTD of the government company. |
| | <u>Sec. 203(5): Penalty:</u> |
| | (a) <u>Company:</u> ₹ 5 lakh |
| | (b) <u>Director & KMP in default:</u> ₹ 50,000 and ₹ 1,000 for each day after the first during which such default continues but not exceeding ₹ 5 lakh. |
| DO Practice - Questions on Sec. 203 | |
| (V) | <u>Sections dealing with Secretarial aspects: Sec. 204 and 205</u> |
| (i) | <u>Secretarial Audit (Sec. 204):</u> |
| | (a) <u>Companies requiring Secretarial Audit [Sec. 204(1)]:</u> |
| | - Every <u>listed company</u> and |
| | - A company belonging to other class of companies as may be prescribed. |
| | Note: Secretarial audit report is to be annexed with the Board's report. |
| | <u>Other class of companies (Rule 9):</u> |
| | (a) Every <u>public company</u> having a paid-up share capital* of \geq ₹ 50 crore; |
| | (b) Every <u>public company</u> having a turnover* of \geq ₹ 250 crore; |
| | (c) Every <u>company</u> having outstanding loans or borrowings* from banks or PFI of \geq ₹100. |
| | *as exist on last date of latest audited F.S. |
| | Note: Format of the Secretarial Audit Report shall be in Form No.MR.3 |

| | |
|--|--|
| | (b) <u>Duty of the company [Sec. 204(2)]:</u> |
| | It shall be the duty of the company to give all assistance & facilities to the CS in practice, for auditing the secretarial and related records. |
| | Note: There is no specific provision in the Act regarding appointment of secretarial auditor, hence the appointment can be made either in Board meeting or general meeting. |
| | (c) <u>Disclosures in Board Report [Sec. 204(3)]:</u> |
| | BOD, in their report u/s 134(3), shall explain in full any qualification or observation or other remarks made by the CS in practice in his report. |
| | (d) <u>Penalty for Contravention [Sec. 204(4)]:</u> |
| | The company, every officer of the company or the CS in practice, who is in default, shall be liable to a penalty of ₹ 2 lakh. |
| | |
| | (ii) <u>Functions of the Company Secretary (Sec. 205):</u> |
| | (a) to report to the Board about compliance with the provisions of this Act, the rules made thereunder and other laws applicable to the company; |
| | (b) to ensure that the company complies with the applicable secretarial standards; |
| | (c) to discharge <u>such other duties</u> as may be prescribed. |
| | ↓ |
| | (1) to provide to the directors, such guidance as they may require, with regard to their duties, responsibilities and powers; |
| | (2) to facilitate convening of meetings and attend Board, committee and general meetings and maintain the minutes of these meetings; |
| | (3) to obtain approvals from the Board, general meeting, government and other authorities as required under the Act; |
| | (4) to represent before various regulators and other authorities in connection with discharge of various duties; |
| | (5) to assist the Board in the conduct of the affairs of the company; |
| | (6) to assist and advise the Board in ensuring good corporate governance |
| | (7) to discharge such other duties as specified under the Act or Rules. |
| | (8) such other duties as may be assigned by the Board from time to time. |
| | DO Practice - Questions on Sec. 204 and 205 |

