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Managerial remuneration – *Provisions in the Companies Bill, 2012*



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At the time of appointment of a managerial personnel, under the current law the remuneration is to be paid in terms of section 309 of the Companies Act, 1956 (the Act) from the profits calculated under section 198 of the Act. Remuneration has not been defined under the Act but section 198 prescribes the constituents of remuneration. In case the Company wants to pay a minimum remuneration keeping in mind the inadequate profits or losses to be incurred it could pay under the Schedule XIII with prior approval of Central Government (CG) as prescribed under the Schedule. However, it is noteworthy that only when the Company decides to make payment in terms of Schedule XIII, relevant provisions and requirements have to be followed to pay such remuneration.

Here we shall have a quick glimpse through the provisions as under the Companies Bill, 2012 (Bill 2012) passed by the Lok Sabha on December 18, 2012 comparing it with the Act, where necessary.

Few important provisions in the Bill 2012

The various sections under the Act have now been compiled under one roof under section 197 of the Bill, 2012. The language is much more simplified. However, there remains one ambiguity in relation to the conditions for paying remuneration at the time of appointment/reappointment of managerial person. Under the Act, only if the remuneration was payable under Schedule XIII, were the conditions applicable to such appointment/reappointment to be followed. Under the Bill, the provisions relating to the appointment have now become part of the law and therefore all the conditions which were previously applicable only while payment under Schedule XIII have now become applicable even if not paid as per Schedule [sec 196].

- Provisions relating to limits on remuneration provided in the existing Act under section 309 with maximum limit of 11% (of net profits) retained. [section 197 of the Bill 2012]
 - The section now specifically uses the word *public* company rather than providing exceptions.
- In case of companies with no profits or inadequate profits, managerial remuneration can be paid
 - As per Schedule of Remuneration (Schedule V – similar to existing Schedule XIII to the Act).
 - If the conditions of such Schedule are not complied with, payment of managerial remuneration will require approval of CG.

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Study of Schedule XIII to the Act vis-à-vis Schedule V to the Bill, 2012

- Section II of Schedule XIII of the Act specifies the amount of remuneration that can be paid by a Company in the event of inadequate profits/losses. The same has para A, B and C limiting the amount of remuneration based on the effective capital and subject to necessary approvals- i.e. either approvals of the shareholders or both of shareholders and Central Government.
- Under Schedule V the limits of the remuneration have been comparatively substantiated in line with the effective capital. The minimum remuneration that can be paid is now Rs. 30 lakh with an effective capital of Rs. 5 crore as against a remuneration of Rs. 75,000 against capital of Rs. 1 crore. It is now expressly clarified that limits to be pro-rated for a period less than one year.
- Para B of Schedule V is amusing rather. The Schedule prescribes that in case the Company does not take Central Government approval it can pay higher of the limits specified under Para A and Para B. Para A lays the table below:

Where the effective capital is	Limit of yearly remuneration payable shall not exceed (Rupees)
Negative or less than 5 crores	30 lakh
5 crores and above but less than 100 crores	42 lakh
100 crores and above but less than 250 crores	60 lakh
250 crores and above	60 lakh plus 0.01% of the effective capital in excess of Rs. 250 crores

Para B however prescribes that in the event the managerial person was not a security holder holding securities of the company of nominal value of rupees five lakh or more or an employee or a director of the company or not related to any director or promoter at any time during the two years prior to his appointment as a managerial person, — *2.5% of the current relevant profit*. Further, such limits shall be doubled if the resolution passed by the shareholders is a special resolution.

- Section III of the Schedule to the Bill, 2012 prescribes for circumstances a company may, without the Central Government approval, pay remuneration

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to a managerial person in excess of the amounts provided in Section II. One of the circumstances is where the company—

- (i) *is a newly incorporated company, for a period of seven years from the date of its incorporation, or*
- (ii) *is a sick company, for whom a scheme of revival or rehabilitation has been ordered by the Board for Industrial and Financial Reconstruction or National Company Law Tribunal, for a period of five years from the date of sanction of scheme of revival,*

it may pay remuneration up to two times the amount permissible under Section II.

Disclosures

- Listed company shall disclose in the Board's report, the ratio of the remuneration of each director to the median employee's remuneration and such other details as may be prescribed [sec 197].
- Remuneration of Directors and Key Managerial Personnel to be now disclosed in the Annual Return [sec 92 (g)]

Nomination and Remuneration Committee

Under the Act the constitution of the Remuneration Committee was an optional requirement unless the Company would have paid remuneration in terms of Schedule XIII. Further, the constitution of such committee was as per Schedule XIII and the notification by Central Government as introduced in the year 2011.

Such committee to constitute of at least three non-executive director(s) with at least one half shall be independent director. The Chairperson of the company (whether executive or non executive) may be appointed as member of nomination and remuneration committee but cannot chair nomination and remuneration Committee. Therefore, the requirement and constitution of such committee is now made specific under the Bill 2012.

Conclusion

Interestingly Para B reads as 2.5% of the current profits- what if the Company is having losses? Seems that at stages the drafting has been done in haste and therefore lot of ambiguity is there in the language. Relaxation to newly incorporated companies is a boon but might have its own disadvantages as well; where the Corporates generally take every advantage of any liberty given by legislation by misusing the privileges and juggling with the provisions of law. On the other hand, the above provisions also aim at better Corporate Governance by disclosure requirements and by mandating the requirement of Remuneration Committee and mandating its composition too is was optional under the current Act for private and unlisted public companies.