# Unit 10: Management of Company

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## Objectives

After studying this unit, you will be able to:

- Describe the legal position of director;
- Outline the qualifications and disqualifications of director;
- Explain the director remuneration;
- Elaborate upon principles of disclosure.

## Introduction

A company, being an artificial person, acts through human agency. Accordingly, under the Act, it is necessary for every company to have a Board of directors. In addition to this, the following categories of managerial personnel may be appointed (s.197-A):

1. Managing Director; or
2. Manager.

Section 197A does not prohibit the employment of other managerial personnel, such as executive or whole-time directors, which do not come within the term "managing director" or "manager". Thus, it is possible for a company to make simultaneously the appointment of (i) managing director and whole time director; or (ii) manager and whole time director. Section 197A prohibits the simultaneous appointment of managing director and manager in the same company.

## 10.1 Directors – Definition and Meaning

Notes

Section 2 (13) defines a Director as including "any person occupying the position of director, by whatever name called." This is a definition based purely on function; a person is a director if he does whatever a director normally does. But the Act gives no further guidance on the function, duties and position of a director. In reality, directors are the persons who direct, conduct, manage or superintend a company's affairs. Section 291 has entrusted the management of the affairs of the company in their hands. They chalk out the general policy of the company within the framework of the memorandum of the company. They appoint the company's officers and recommend the rate of dividend. The directors of company are collectively referred to as the 'Board of Directors' [s. 2(6)].

Thus, it is not the name by which a person is called but the position he occupies and the functions and duties which he performs that determine whether he is a director of a company or not. In Forest of Dean Coal Mining Co. Re (1878) 10 Ch D 450, it was stated that function is everything; name matters nothing. So long as a person is duly appointed by the company to control its business and authorised by its articles to contract in its name and on its behalf, he is a director, whether named as such or not.

The articles of a company, sometimes, designate its directors as governors, members of the governing council or the board of management or may give them any other title, but so far as the law is concerned they are simply directors. For example, in the case of associations registered as companies under s. 25, the members of the executive committee or governing council or management board are directors for purpose of the Act, even when they are not designated as directors.

### 10.1.1 Deemed Director (s. 7).

For certain purposes, a person even when he is not a director may be deemed to be a director of a company. The Act treats as director a person in accordance with whose directions or instructions the Board of directors of a company is accustomed to act. This provision has the effect of widening the definition of the term 'director'. However, this provision merely operates to impose liabilities or prohibition on such a person who is deemed to be a director. However, a deemed director does not acquire any right or power in connection with the management of the company. He may be made liable but he cannot demand to participate in the meetings of the Board of directors or to manage the affairs of the company in any way. But for the purpose of treating a person as a deemed director and invoking his liability, it is necessary to establish that the Board of directors is accustomed to act according to his directions and instructions. Acting casually or once in a while on certain instructions by a person would not be a 'deemed director'.

A deemed director need not necessarily be an individual. The person may even be a body corporate say, a holding company.

It must be noted that the expression 'deemed director' does not include persons advising the Board of directors of a company in their professional capacity. Thus, a lawyer, accountant or other professional advisor will not come within the expression 'deemed director' when he gives professional advice or instructions and the Board is accustomed to act according to his advice or instructions, then he will not be a 'deemed director'.

Section 303(1) provides that any person with whose directions or instructions the Board of directors of a company is accustomed to act is also deemed to be a director.

A manager or any other managerial personnel is, however, not a director [Deen Dayalu v. Sri B. P. Reddy A.P. (1984) 2 Comp LJ 396].

A 'deemed director' is called as 'shadow director' under English Law.

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### 10.1.2 Small Shareholders' Director

A public company having (a) a paid up capital of five crore rupees or more, and (b) one thousand or more small shareholders may have a director elected by such small shareholders in the manner as may be prescribed. For this purpose, "small shareholder" means a shareholder holding shares of nominal value of twenty thousand rupees or less (i.e. up to ₹ 20,000) in a public company to which this section applies. The Department of Company Affairs, has prescribed the Companies (Appointment of the Small Shareholders' Director) Rules, 2001. Such a director will be elected by the majority of the small shareholders. The tenure of such director shall be a maximum of three years and he need not retire by rotation. However, he can be re-elected for a period of three years on the expiry of his tenure. Such a director can be removed in pursuance of s. 284. A person cannot hold office as small shareholders' director in more than 2 companies. Further, the person proposed to be elected must be a small shareholder of the company. Furthermore, such a director is not eligible for appointment as whole time or managing director of the company. If he ceases to be a small shareholder, he is deemed to have vacated his office as 'small shareholders director'.

*Example:* The Board of directors of ABC Ltd., an unlisted company, having a paid up share capital of ₹ 6 crores consisting of equity share capital of ₹ 5 crores and preference share capital of ₹ 1 crore and also having 11,000 small shareholders holding equity shares propose to appoint a director to represent the small shareholders.

Under s. 252, a public company, if it has a paid up capital of ₹ 5 crores or more, and one thousand or more small shareholders may have a director elected by such small shareholders. It is obvious, that the appointment of such a director is not mandatory; it is discretionary for the company.

*Example:* In a company, there are more than one thousand small shareholders, and it has a paid up capital of more than five crore rupees. The small shareholders have exercised their right to appoint a director on the board of the company. The company wants to remove him before the expiry of his period of appointment. The company can do so under s. 284 without the consent of the small shareholders.

## 10.2 Legal Position of Directors

The exact position of 'Director' is hard to define, as no formal definition, either statutory or judicial, of the term has been given. However, judicial pronouncements have described them as (i) agents, (ii) trustees, or (iii) managing partners. But each of these expressions is used not as exhaustive of their power and responsibilities but as indicating points of view from which they may for the moment and for the particular purpose be considered.

### 10.2.1 Directors as Agents

The directors act as agents of the company and the ordinary rules of agency apply. They exercise the powers that are subject to the duties within the framework of the company's articles, and the Act. For instance, they may make contracts on behalf of the company and they will not be personally liable as long as they act within the scope of their authority. But if they contract in their own name, or fail to exclude personal liability, they also will be liable. If the directors exceed their authority, the same act may be ratified by the company. But if they do something beyond the objects clause of the company, then the act is *ultra vires* and the company cannot ratify the same. But directors are not agents for the individual shareholders; they are the agents of the company – the artificial person.

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### 10.2.2 Directors as Trustees

The directors have also been described as trustees. But they are not trustees in the full sense of the term, in as much as no proprietary rights of the company's property are transferred to them and, therefore, they enter into contracts on behalf of the company and in the name of the company. On the other hand, in the case of a trust, the legal ownership of the trust property is transferred to the trustee and therefore, he can enter into contract in his own name, but whatever he does, he does for the benefit of the beneficiaries.

Although directors are not trustees in the real sense of the term, they occupy an office of trust and are in certain respects in the position of trustees for the company. Such cases are:

- They are trustees of money which comes to their hands or which is actually under their control. If they mis-apply company's money, they have to make good the same as if they were trustees.
- They are trustees for exercising powers conferred on them for the benefit of the company. For instance, powers to allot shares, to make calls, or to forfeit shares should be exercised bona fide in the interests of the company.
- They stand in a fiduciary relationship to the company and, therefore, whenever there is clash of his personal interests with that of the company, he should keep in mind the company's interests.

A director is in no way a trustee for individual shareholders except when the former induces the latter by mis-representation to sell the shares to him.

### 10.2.3 Directors as Managing Partners

The directors are also sometimes described as managing partners. In this sense, a company is considered a partnership firm. As one or more partners may manage the affairs of the firm on behalf of all the partners, similarly a few shareholders, who are elected directors by the shareholders, manage the affairs of the company. They manage the affairs of the company on their own behalf and on behalf of other shareholders who elect them.

### 10.2.4 Directors as Employees of the Company

The directors are not employees of the company or employed by the company, nor are they servants of the company, or members of the "company's staff". A director can, however, hold a salaried employment or an office in addition to that of his directorship which may, for these purposes, make him an employee or servant and in such a case, he would enjoy rights given to employees as such; but his directorship and his rights through that directorship are quite separate from his rights as employee. Thus, he is then entitled to remuneration and other benefits admissible to him as an employee in addition to his remuneration as director under the Act. The Act recognises situations of this nature. Sections 314 and 318, for instance, provide for a director holding an office or place of profit under a company.

### 10.2.5 Director as Officers of the Company

Directors are treated as officers of the company [s. 2(30)]. Also, directors are 'officers in default' (s. 5) and may become liable to certain penalties for failure to comply with certain provisions of the Act.

Notes

### Self Assessment

Fill in the blanks:

1. ..... defines a Director as including "any person occupying the position of director, by whatever name called."
2. A ..... need not necessarily be an individual.
3. A 'deemed director' is called as 'shadow director' under .....
4. The directors act as agents of the company and the ordinary rules of ..... apply.
5. In partnership firm, the directors are also sometimes described as .....

## 10.3 Qualifications and Disqualifications of Directors

The Act has not prescribed any academic or professional qualifications for the directors. Also, the Act imposes no share qualification on the directors. So, unless the company's articles contain a provision to that effect, a director need not be a shareholder unless he wishes to be one voluntarily. But the articles usually provide for a minimum share qualification. Thus, Regulation 66 of Table A provides that a director must hold at least one share in a company. Where a share qualification is fixed by the articles of a company, the Act provides (s. 270) that:

- It must be disclosed in the prospectus;
- Each director must take his qualification shares within two months after his appointment;
- The nominal value of the qualification shares must not exceed ₹ 5,000 or the nominal value of one share where it exceeds ₹ 5,000;
- Share warrants will not count for purposes of share qualification.

If a director fails to obtain his share qualification within two months, he vacates office automatically on the expiry of two months from the date of his appointment and if he acts as director after the expiry of two months without taking the qualification shares, he is liable to a fine up to ₹ 5,000 for every day until he stops acting as such (s. 272).

However, the articles of a company can neither compel a person to hold qualification shares before he is elected a director nor can they require him to obtain qualification shares within a shorter period than two months after his appointment and if any provisions to this effect is made in the articles, it shall be void.

The effect of this provision is that if the company is wound up during this period of two months, the director cannot be placed in the list of contributories, in as much as there is no express or implied contract under which he would be bound to take the qualification shares, since his name cannot be put on the register of members unless he has applied for shares and these are allotted to him [Zamir Ahmed Raz. vs. D.R. Banaji (1957) 27 Comp. Cas. 634].

*Task* X Co. Ltd. wants to make a contract with a partnership firm. Four of the five directors of the company are partners of such partnership. How can the contract be executed? [***Hint:*** The contract may be executed by the general body of shareholders by passing an ordinary resolution to that effect. Also see s.299.]

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However, the mere acting as a director does not import any agreement to take the shares from the company; but, if in such circumstances he is put on the register by the officers of the company after the time limit for qualifying has expired (i.e. 2 months after his appointment) and he continues to act as a director, he is estopped by his conduct from repudiating the shares and will be liable to pay for them.

The appointment of a director commences from the date on which the result of poll taken to elect is announced, and the two months are calculated from that date, and not the one on which the poll was actually taken.

It may be noted that:

- The qualification shares can be held by a director even as a trustee, if that fact does not appear on the register of members, and if the company can deal with the shares as his own.
- Also, shares held jointly with any other person is sufficient share qualification. It was held in Grundy v. Briggs [1910]1 Ch. 444, that unless articles provide otherwise, shares in joint names entitles any of the joint holders to be appointed as a director. But not more than one joint holder can be appointed.
- The mortgaging of shares does not disqualify a person to be appointed as a director, unless the articles provide otherwise.
- A person who holds requisite qualification shares at the time of his appointment, a subsequent increase in the amount of share qualification cannot be made applicable to him [International Cable Co. Re, (1892) 66 LT 253].

Where a director acts without acquiring his qualification shares after the expiry of two months from the date of his appointment, the company will be bound to third parties for acts of such a director until the defect in appointment or disqualification is disclosed, and acts done by him after the disclosure by the company will not bind it. Thus a de facto director is as good a director as a *de jure* director so far as persons having no notice of the defect are concerned (s. 290).

As the provisions of s. 270 and s. 272 do not apply to a private company (s. 273), it may or may not provide in its articles any requirement of share qualification. The articles may thus provide for share qualification and the amount may be more than ₹ 5000.

Further, a private company which is not a subsidiary of a public company may, by its articles, provide additional qualifications for a director, such as, a person must be a B. Com., or holding a fixed deposit receipt in his own name issued by the company.

Section 274 has laid down certain disqualifications and therefore, the following persons are incapable of being appointed directors of any company:

1. A person found by a court to be of unsound mind;
2. An un-discharged insolvent;
3. A person who has applied to be adjudged an insolvent;
4. A person who has been convicted by a court for an offence involving moral turpitude and sentenced in respect thereof to imprisonment for not less than six months and a period of five years has not elapsed from the date of the expiry of the sentence;
5. A person who has failed to pay calls on shares held by him whether alone or jointly with others for six months from the date fixed for the payment;
6. A person who has been disqualified by court under s. 203 which empowers the court to restrain fraudulent persons from managing companies, unless the leave of the court has been obtained for his appointment;

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7. Such person is already a director of a public company which, (a) has not filed the annual accounts and annual returns for any continuous three financial years; or

8. Has failed to repay its deposit or interest thereon on due date or redeem its debentures on due date or pay dividend, and such failure continues for one year or more. Further, such person shall not be eligible to be appointed as a director of any other public company for a period of 5 years from the date on which such public company, in which he is a director, failed to file annual accounts and annual returns under (a) above or has failed to repay its deposits or interest or redeem its debentures on due date or pay dividend referred to in (b).

The disqualifications mentioned under (iv) and (v) above may be removed by the Central Government by a notification in the official gazette. On the other hand, a private company may provide in its articles that a person shall be disqualified for appointment as director on any other additional ground. However, a subsidiary private company or a public company cannot, by its articles, provide for any additional disqualifications.

### 10.3.1 Other Disqualifications

The following two provisions also provide for disqualifications of directors:

(i) Where a director has been convicted of an offence under s. 209A, he shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such. On such a vacation of office, he shall be disqualified for holding the office of a director in any company for a period of five years from such date.

(ii) A director who has been removed from any managerial position by the Central Government shall not be a director of a company, for a period of five years from the date of the order of removal unless the said Government has reduced the period with the concurrence of the Company Law Board [s, 388 E].

### 10.3.2 Minor as a Director

In the case of a minor, though there is no provision in the Act, expressly disqualifying him, as he is not competent to contract, he cannot file either with the company or with the registrar any valid consent to act as director, as required by s.264. But as s.264 applies only to public companies; there is nothing prohibiting a minor being a director of a private company. However, from a practical point of view a minor can be an ornamental director as he can neither be party to any transaction which requires competency to contract – nor, for the same reason, can he be delegated any powers of the board. He may possibly vote on all resolutions at board meetings.

*Example:* Mr. Ram is a director of ABC Ltd. XYZ Ltd. and PQR Ltd. ABC Ltd. was regular in filing annual returns, but did not file annual accounts for the year ended March 31, 2007.

Further ABC Ltd. failed to pay interest on loans taken from a public financial institution from 1st January, 2007 onwards and also failed to repay the matured deposits on due date from 1st April, 2007 onwards.

Mr. Ram is proposed to be appointed as additional director of MN Ltd. on 1st June, 2008.

Also Mr. Ram wants to continue as a director of XYZ Ltd. and PQR Ltd. Further, he seeks reappointment when he retires by rotation at the AGM, of respective companies to be held in September, 2008.

Notes

As regards failure of ABC Ltd. to pay interest on term loans taken from a public financial institution, the disqualification does not apply under s. 274(1)(g)(B).

As regards failure to repay its deposits on due date and the failure continues for more than one year, Mr. Ram is disqualified. In the light of this disqualification, he is not eligible to be appointed on additional director in MN Ltd. From 1st June, 2008 onwards.

The disqualification would come into operation only at the time of appointment or reappointment of Mr. Ram as director of any public company after the default has become effective. Till such time, he can continue to hold office of director in all public companies in which he is a director. Therefore, he need not vacate the office of director in XYZ Ltd. and PQR Ltd. (either under s. 274(1)(g) or s. 283).

However, Mr. Ram cannot seek reappointment in XYZ Ltd. and PQR Ltd. when he retires by rotation at the AGMs to be held in September, 2008.

*Example:* Mr. A is a director of ABC Ltd. which failed to repay matured deposits from 1st April, 2007 onwards and the default continues. But ABC Ltd. is regular in filing annual accounts and annual returns. Mr. A is also a director of PQR Ltd. and XYZ Ltd.

ABC Ltd. has committed default under s. 274 (1)(g)(B) and Mr. A, being a director of ABC Ltd. becomes disqualified for his appointment or reappointment as a director in any other public company. However, he need not vacate his office of directors in PQR Ltd. and XYZ Ltd. as it is not required either by s. 274 or s. 283.

In case DEF Ltd. wants to appoint Mr. A as an additional director at the Board meeting to be held on 15 May, 2008, it cannot be done [Proviso to s. 274(1)(g)].

Further, if Mr. A had ceased to be a director of ABC Ltd. by resignation on 1st March, 2008, then the proviso to s. 274(1)(g) would not be attracted, and therefore he could be appointed as a director in DEF Ltd.

*Example:* The articles of association of MKP Ltd. incorporated with an authorised share capital of ₹ 50 crores divided into 5 crore equity shares of ₹ 10 each contained the following clause:

"The qualification of a director shall be the holding of at least 1,000 equity shares in the company and such a director, if not already so qualified shall have to obtain his qualification within a period of 30 days from the date of his appointment as a director."

A person appointed as a director may acquire shares for qualification within 2 months after his appointment. Therefore, the clause requiring him to obtain his qualification shares within a period of 30 days from the date of his appointment is void.

In this case, the disqualification specified in s. 274(1)(g)(A) does not apply as ABC Ltd., has not committed defaults in respect of both the matters (i.e. annual returns and annual accounts for three consecutive financial years).

Also, the clause requires him to hold at least 1,000 equity shares of ₹ 10 each. This amounts to ₹ 10,000 whereas s. 270(3) restricts the nominal value of the qualification shares to ₹ 5000 or nominal value of one share where it exceeds ₹ 5000.

*Example:* Mr. A, who has huge personal liabilities far in excess of his assets and properties, has applied to the court for adjudicating him as an insolvent and such application is pending. He cannot be appointed as a director of a company [s. 274(1)(c)].

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*Example:* Mr. B was caught red handed in a shop lifting case two years ago and for embezzlement of funds and sentenced to imprisonment for a period of eight weeks. He can be appointed as a director of a company, as the disqualification given in s. 274(1)(d) is not attracted.

*Example:* Mr. C, a former bank executive, was convicted by a court eight years ago for embezzlement of funds and sentenced to imprisonment for a period of one year. He can be appointed as a director of a company as disqualification under s. 274(1)(d) is not attracted.

*Example:* Mr. D is a director of DLT Ltd. which has not filed its annual returns pertaining to the AGMs held in the calendar years 2005, 2006 and 2007. He can be appointed as a director in any other company under s. 274(1)(g), as the failure on the part of DLT Ltd. is on account of annual returns, and not in respect of filing of annual accounts.

The provisions of s. 274 regarding disqualifications of directors do not apply in the following cases:

(i) The special directors appointed on the board of a company under the Sick Industrial Companies (Special Provision) Act, 1985;

(ii) The nominee directors appointed on the board of a company by public financial institutions and companies established by the Special Acts of Parliament, like I.D.B.I., L.I.C., U.T.I.

(iii) The nominee directors appointed by the Central or State Government on a banking company.

### 10.3.3 Validity of acts of Directors (s. 290)

Section 290 provides that the acts done by a director shall be valid even if his appointment is discovered to be invalid because of any defect or disqualification or where his appointment had terminated by virtue of any provisions contained in the Act or in the articles. Section 290 is designed to protect persons dealing with the company such as lenders, vendors and purchasers of shares and debentures. Thus, a party entering into a contract with a company through its director may assume that the acts of the director are valid if he does not know the irregularity, if any, in the appointment of the director.

However, the acts will not be valid (or the provisions of s. 290 shall not operate) where:

(i) His appointment is illegal, or there is no appointment at all.

(ii) He continues in his office knowing that his term has expired.

(iii) He knew from the beginning that his appointment was defective.

(iv) He acted in the capacity of a managing director, manager [subject, however, to the provisions of s. 269(12)] or secretary.

(v) His acts are ultra vires the company.

(vi) Where requirement as to minimum number of directors is not satisfied.

(vii) The third party was aware of the defect in his appointment.

Notes

## 10.4 Appointment of Directors

The appointment of directors rests in the following hands:

1. Subscribers to the memorandum – s.254; Clause 64 (Table A);
2. Company in general meeting – Ss.255-57; 263-265;
3. Board of directors – Ss.260, 262, 313;
4. Central Government – s.408; (e) Third parties – s.255.

### 10.4.1 Appointment of First Directors

The first directors are usually named in the articles of a company. The articles may, however, instead of naming the first directors confer power on the subscribers, or majority of them, to appoint the directors. Where the appointment is to be made by the majority of subscribers, the majority of them (and not only the quorum fixed by the articles) should be present if the appointment is to be valid. Where there are no articles or the articles neither name them nor confer any such power on the subscribers, then Clause 64 of Table A in Schedule I to the Act confers powers on the subscribers or a majority of them to make the appointment of first directors. Furthermore, if the articles neither name them, nor do they contain a provision for their appointment by the subscribers and Table A is excluded, then the subscribers to the memorandum who are individuals are deemed to be the first directors of the company until the directors are duly appointed at a general meeting of the company in accordance with the provisions of s.255.

### 10.4.2 Appointment of Subsequent Directors

Sections 255 and 265 provide for three alternate schemes for the constitution of the Board of directors of a public company or a private company which is subsidiary of a public company. These schemes are: (i) all the directors retire at every annual general meeting [s.255]; or (ii) at least two-thirds of the total number of directors must be persons whose period of office is liable to determination by retirement by rotation (s.255); or (iii) at least two-thirds of the directors may be appointed by the principle of proportional representation, by a single transferable vote by a system of cumulative voting or otherwise and shall be directors for a period of three years at a time (s.265). The remaining directors in (ii) and (iii) and the directors generally of a pure private company, unless otherwise provided in the articles, must also be appointed by the company in general meeting.

Thus, a company may have two types of directors, retiring and non-retiring. The directors may retire by rotation as given in s. 256 or after a period of 3 years as given in s. 265.

Thus, every company should have a duly constituted board appointed in accordance with the provisions of s.255. A general meeting is called by the 'first' directors after the allotment of shares in the case of a company limited by shares and in the case of any other company, after its incorporation, for the specific purpose of appointment of directors.

### 10.4.3 Restrictions on Appointment of Directors

Section 266 states that a person cannot be appointed a director by the articles, or named as a director in the prospectus or statement in lieu of prospectus unless, before registration of the articles, publication of the prospectus, or filing of the statement in lieu of prospectus, he has:

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Signed and filed with the registrar a consent in writing to act as such director; and either:

(i) Signed the memorandum for his qualification shares, if any; or

(ii) Taken his qualification shares, if any, from the company and paid or agreed to pay for them; or

(iii) Signed and filed with the registrar a written undertaking to take from the company his qualification shares, if any, and pay for them; or

(iv) Made and filed with the registrar an affidavit to the effect that his qualification shares are registered in his name.

This section does not apply to:

- A company not having a share capital;
- A private company;
- A public company which was formed as a private company;
- A prospectus issued by a company after the expiry of one year from the date on which the company was entitled to commence business.

### Self Assessment

6. The agenda of the first Board Meeting of a limited company generally consists of the following items:

   (i) Election of chairman

   (ii) Approval of draft prospectus

   (iii) Appointment of officers, viz., The secretary, the manager and the accountant

   (iv) Incorporation of the company and the legal advisor to report on the same

   The correct order in which the above items of the agenda usually appear is:

   (a) (i), (ii), (iii), (iv) (b) (iv), (iii), (ii), (i)

   (c) (iii), (iv), (i), (ii) (d) (iv), (i), (iii), (ii)

7. Which one the following statements relating to a company secretary are not correct?

   (a) He is not likely to perform duties towards shareholders

   (b) He is the mouthpiece of the Board of directors

   (c) He may be considered to be the head of the administrative section of a company

   (d) He is to arrange for Board meetings.

## 10.5 Modes of Appointments

The Companies Act does not prescribe how directors are appointed; this is left to the companies' articles of association. Typically, directors are elected by the members at the annual general meeting of the company.

Table A which contains default articles makes provision for the appointment of directors. Thus, the present position is that the company's articles will provide for the appointment of directors, or the default position in Table A will apply unless Table A is excluded by the company's articles.

Notes

Having an express provision in the Companies Act will simplify matters as a company will not have to provide for the appointment of directors in its articles or rely on Table A, unless the company wishes to provide for a different mode of appointment. The Steering Committee received industry feedback that in practice, Table A is often excluded by the companies' articles as it is not found to be useful.

The current Singapore approach of not prescribing in legislation how directors are appointed is consistent with the position in the UK and Hong Kong. The Steering Committee considered whether the Companies Act should expressly provide for the mode of appointing directors, following the position in Australia and New Zealand.

For reasons of simplicity and greater clarity, the Steering Committee recommends that the Companies Act should provide expressly that unless the articles provide otherwise, a company may appoint a director by ordinary resolution passed at a general meeting. The mode of appointment is subject to the company's articles to give flexibility to companies.

This approach is consistent with that in Australia where the statutory provisions in the Australia Corporations Act 20017 on the mode of appointing directors are replaceable rules. It is also consistent with the approach in the New Zealand Companies Act 1993 where section 153(2) provides for the appointment of subsequent directors by ordinary resolution, unless the constitution of the company otherwise provides.

During the focus group consultation, the majority of the respondents expressed support for having such an express provision on the appointment of directors in the Companies Act. It was felt that notwithstanding that there is little dispute in practice on how directors are appointed, it would be good to clearly provide that the general meeting has power to appoint directors, subject to contrary provision in the articles.

## 10.6 Director Remuneration

Section 198 provides that the total managerial remuneration payable by a public company or a private company which to its directors or manager in respect of any financial year must not exceed 11 per cent of the net profit of that company for that financial year, in computing the above ceiling of 11 per cent computed in the manner laid down in section 349 and 359. The fees payable to directors for attending Board meetings is not included.

### 10.6.1 What is included in Remuneration?

Explanation to s.198 describes the term 'remuneration'. According to it, for the purposes of Ss. 309, 310, 311, 381 and 387, 'remuneration' includes the following:

1. Any expenditure incurred by the company in providing rent-free accommodation, or any other benefit or amenity in respect of accommodation free of charge, to any of its directors or manager;
2. Any expenditure incurred by the company in providing any other benefit or amenity free of charge or at a concessional rate to any of the persons aforesaid;
3. Any expenditure incurred by the company in respect of any obligation or service, which, but for such expenditure by the company, would have been incurred by any of the persons aforesaid; and
4. Any expenditure incurred by the company to effect any insurance on the life of, or to provide any pension, annuity or gratuity for, any of the persons aforesaid or his spouse or child.

Notes

Section 309 contemplates three kinds of directors, i.e., (i) Managing Director; (ii) Whole-time director; (iii) Director pure and simple. Further, s.309 provides that subject to the general provisions of s.198, dealing with the total managerial remuneration, the remuneration be determined by the articles, or by a resolution or, if the articles so require, by a special resolution, passed by the company in general meeting. Any remuneration paid for services in any other capacity shall not be included if: (a) the services rendered are of a professional nature; and (b) in the opinion of the Central Government, the director possesses the requisite qualifications for the practice of the profession.

A director who is neither in the whole-time employment of the company nor a managing director may be paid remuneration. (a) by way of a monthly, quarterly or annual payment with the approval of the Central Government; or (b) by way of commission, if the company by special resolution authorises such payment; or (c) by both.

*Task* X holds shares and directorship in a number of companies. X is proposed to be a Director of a company named Asian Ltd. State the requirements of law necessary to be complied with by him before and after he joins the Board of Asian Ltd. [***Hint:*** (i) X should resign one of the directorships, if he is already a director of more than 15 companies, (ii) He should give his consent in writing before joining the Board of Asian Ltd. (s.264) (iii) He should file his consent with the Registrar within 30 days of the date of joining. (iv) He should disclose the nature and extent of his interest in other companies (s.299). (v) He should acquire the qualification shares, if any prescribed by the Articles of Asian Ltd. in case he does not own the same already.]

However, in either of the above cases, the remuneration paid to such director, or where there is more than one such director, shall not exceed: (i) one per cent of the net profit of the company, if the company has managing or whole-time director or manager; (ii) three per cent of the net profits of the company in any other case. The company in general meeting may, however, with the approval of the Central Government, authorise the payment of a commission at a rate higher than one per cent, or as the case may be, three per cent of its net profits.

Each director is entitled to receive a sitting fee for each meeting of the Board or a committee thereof, provided the same is authorised by the articles.

A whole-time director or a managing director may be paid remuneration either by way of a monthly payment or at a specified percentage of the net profits of the company or partly by one way and partly by the other; provided that except with the approval of the Central Government such remuneration shall not exceed 5 per cent of the net profits for one such director and if there is more than one such director, 10 per cent for all of them together. Furthermore, a managing or whole-time director who is in receipt of any commission from the company cannot receive any remuneration from any subsidiary of the company.

If any director draws or receives, directly or indirectly, by way of remuneration any sum in excess of the limits stated above, without the sanction of the Central Government, where it is required, he shall have to refund such sums to the company and until the refund is made the money will be held by him in trust for the company. The company cannot waive the recovery of any sum refundable to it, unless permitted by the Central Government.

The provisions of s.309 will not apply to a private company unless it is a subsidiary of a public company.

Notes

### 10.6.2 Increase in Remuneration

Section 310 provides that every increase in the remuneration of any director including a managing or whole-time director granted or provided by any amendment in his term of appointment which has the effect of increasing, whether directly or indirectly, the amount payable to him would not be operative unless the same has been approved by the Central Government. But no approval of the Central Government would be required if the increase in remuneration made is in accordance with the conditions specified in Schedule XIII. Also no approval of the Central Government is necessary, if the increase in the remuneration is only by way of fee for each meeting of the Board or a committee of the Board attended by any such director and the amount of the fee after such increase does not exceed such sum as may be prescribed. The Central Government has laid down differential scale of sitting fee according to the paid-up capital of the companies.

## 10.7 Remuneration Payable to a Manager

Section 387 provides that he may receive remuneration either by way of a monthly payment or by way of a specified percentage of the 'net profits' of the company, or partly by one way and partly by the other. Such remuneration, however, must not exceed in the aggregate 5 per cent of the net profits except with the approval of the Central Government.

### 10.7.1 Managerial Remuneration vis-à-vis Schedule XIII

A public company is entitled to appoint its managerial personnel and fix their remuneration so long as the same is in accordance with the conditions laid down in Schedule XIII without seeking the prior approval of the Central Government. Schedule XIII, provides as follows:

1. ***Remuneration Payable by Companies Having Profits:*** Subject to the provisions of s.198 and s.309, a company having profits in a financial year may pay any remuneration, by way of salary, dearness allowance, perquisites, commission and other allowances, which shall not exceed 5 per cent of its net profits for one such managerial person and if there are more than one such managerial persons, 10 per cent for all of them together.
2. ***Remuneration payable by companies having no profits or inadequate profits:*** Where in any financial year during the currency of tenure of the managerial person, a company has no profits or its profits are inadequate, it may pay remuneration to a managerial person, by way of salary, dearness allowance, perquisites and other allowance, not exceeding ceiling limit of ₹ 24,00,000 per annum or ₹ 2,00,000 per month calculated on the following scale:

| Where the effective capital of the company is | Monthly remuneration payable shall not exceed (₹) |
|---|---|
| Less than ₹ 1 crore | 75,000 |
| ₹ 1 crore or more but less than ₹ 5 crores | 1,00,000 |
| ₹ 5 crore or more but less than ₹ 25 crores | 1,25,000 |
| ₹ 25 crore or more but less than ₹ 50 crores | 1,50,000 |
| ₹ 50 crore or more but less than ₹ 100 crores | 1,70,000 |
| ₹ 100 crores or more | 2,00,000 |

In addition to the above, certain perquisites like contribution to provident fund, gratuity, leave encashment may be paid. Non-resident Indians may also be paid children education allowance,

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holiday passage for children studying outside India or family staying abroad, leave travel concession. These additional benefits shall be subject to the limits laid down in Schedule XIII.

The expression 'effective capital' shall mean the aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account, reserves and surplus (excluding revaluation reserve); long term loans and deposits repayable after one year (excluding working capital loans, overdrafts, interest due on loans unless funded, bank guarantee, etc. and other short term arrangements) as reduced by the aggregate of any investments (except in case of investments by an investment company whose principal business is acquisition of shares, stock, debentures or other securities), accumulated losses and preliminary expenses not written off.

**Sitting Fee (s.310)**

The sitting fee payable to a director for each meeting of the Board of Directors or a committee thereof shall not exceed ceiling prescribed by the Central Government (presently, ₹ 5,000). Any increase in the sitting fee payable to a director shall not require the prior approval of the Central Govt. if it falls within the prescribed limits.

## 10.8 Disclosure

Disclosure of interest by directors, Section 299 provides as follows:

1. A director of a company who is in any way concerned or interested in a contract or arrangement by or on behalf of the company must disclose such concern or interest at the board meeting at which the contract is discussed. However if the director was not interested in the contract at the date of the meeting, then he must disclose his interest at the next board meeting held after he became interested.
2. However, if a director gives a general notice to the board that he is a director or member of a specified company or firm and is to be regarded as interested in any contract which is made with, it then this is a sufficient declaration or disclosure of interest. Such a general notice must, however, be given once every financial year and that too at the board meeting.
3. Non-compliance by a director with the aforesaid requirements will render him liable to a fine up to ₹ 50,000.
4. However, there is an exclusion clause. All contracts and arrangements between two companies where the interest of a director or director of one company in the other does not exceed a shareholding of two percent of the paid-up share capital of the other are excluded from the provisions of s.299.

Section 299 is in accordance with the principle of law that an agent cannot put himself into a position where his duty and his interest conflict.

### 10.8.1 Interested Directors not to Participate or Vote in Board's Proceedings

Section 300 provides as follows:

"An interested director must not participate in the discussions or exercise his vote on the particular contract or arrangement in which he is interested. If he does vote, his vote shall be void, nor his presence count for the purposes of quorum".

Notes

However, these restrictions do not apply to:

1. A private company which is neither a subsidiary nor a holding company of a public company;
2. A private subsidiary company in respect of contracts or arrangements entered into by it with the holding company;
3. Any contract of indemnity against any loss which any director(s) may suffer by reason of becoming or being a surety or sureties for the company;
4. A company in which the director had only his qualification shares and he was nominated as a director by the other company with which the contract is entered into;
5. A company in which the director is a member holding not more than two per cent of the paid-up share capital of the company.

A director who knowingly contravenes the provisions of s.300 is liable to be fined up to ₹ 50,000.

### 10.8.2 Register of Contracts in which Directors are Interested

To ensure that the provisions of sections 297-300 are complied with, s.301 provides as follows:

1. Every company must keep one or more registers in which must be entered separately particulars of all contracts or arrangements in which directors and their relatives are interested, and also particulars of firms and companies in which directors are interested as partners, members or directors. The particulars to be entered in the register are:
   (i) The date of the contract or arrangement;
   (ii) The names of the parties thereto;
   (iii) The principal terms and conditions thereof;
   (iv) The date on which the contract was placed before the board, where it is required to be placed;
   (v) The names of the directors voting for and against the contract or arrangement; and
   (vi) The names of directors who remained neutral.
2. The aforementioned particulars must be entered in the register within seven days of the approval of the board, where approval is required.

   In case of any other contract or arrangement, the particulars must be entered in the register within seven days of the receipt at the registered office of the company of the particulars of such other contract or arrangement or within 30 days of the date of such contracts or arrangements whichever is later.

   The register is required to be placed before the next meeting of the board and is then to be signed by all the directors present at the meeting.
3. The register aforesaid shall also specify, in relation to each director of the company, the names of the firms and bodies corporate of which notice has been given by him under s.299.
4. Exemption has been granted to contracts for the sale or purchase or supply of goods, etc. not exceeding ₹ 1000 in value in any year, and also to contracts by banking companies for collection of bills in the ordinary course of business, and transactions of banking and insurance companies in the ordinary course of business with any director, relative, partner, etc.

Notes

5. If default is made in complying with the above provisions of s.301, then the company, and every officer of the company who is in default, shall, in respect of each default, be punishable with fine which may extend to ₹ 5000.

6. The above register shall be kept at the registered office of the company, and it shall be open to inspection. Extracts may be taken from the register and any member of the company may demand copies thereof. The provisions of s.163 which apply to the register of members shall apply to the register in which directors are interested.

*Task* The total strength of the Board of directors of a company is ten. How many directors are liable to retire by rotation at the next annual general meeting? [*Hint:* Three] (s. 255,256)

### 10.8.3 Disclosure of Director's Interest in Contract Appointing Manager, or Managing Director

Section 302 states that where a company appoints or varies the terms of appointment of a manager, managing director, or whole-time director, and any director is directly or indirectly interested or concerned in the matter, then an abstract of the matter and of the director's interest therein should be circulated by the company to its members within 21 days of the date of the contract or its variation. These contracts must be kept at the registered office of the company, and must be available for inspection by the members. If the appointment or variation is made by a resolution of the board, the above provisions will apply to the same.

If default is made in complying with these provisions, then the company, and every officer of the company who is in default, shall be punishable with fine which may extend to ₹ 10,000.

Further, all contracts entered into by a company for the appointment of a manager, managing director shall be kept at the registered office of the company and shall be open to the inspection of the members of the company. Extracts may be taken from the register and copies thereof may be demanded by any member. The provisions of s.163, which applies to the register of members become applicable here also.

Summary of provision of Section 297 with respect to interested directors:

| Particulars | Persons in which director is said to be interested | Approvals required |
|---|---|---|
| Contracts with the company | 1. Director or relative<br>2. A firm in which a director or his relative is a partner.<br>3. Any other partner in such a firm<br>4. A private company of which the director is a director or a member. | 1. Approval of the board.<br>2. In case the PUC of the company is ₹ 1 crore or more, then approval of the board and prior approval of the central government. |

*Example:* R is the managing director of a public company with a paid up capital of ₹ 200 lac. He is also a partner of the firm in which the other partners are his wife and two sons. The company proposes to enter into a contract with the firm for the sale of its products of the value of ₹ 5 lac on credit.

As per s.297 such a contract can be entered only if (i) the consent of board of directors is obtained, and (ii) the previous approval of the central government is obtained (since the paid up capital is more than ₹ 1 crore).

Notes

*Example:* P is the managing director of a public company with a paid up capital of ₹ 150 lac. The company proposes to enter into a contract for the sale of its products of the value of ₹ 5 lakhs on credit with a private company in which the wife of P and his two sons S and T are members.

The facts of this case do not attract the restriction for entering into contract with an interested director. P is neither a director nor a member of the private company.

*Example:* The articles of a company states that a director shall not vote in respect of a contract in which he is interested. In a resolution put up for approval of the shareholders, a shareholder (even if he is a director), may vote as he pleases even when his interests are different from or opposed to those of the company. As a shareholder, he is not a trustee for the company or for any one else. Hence, the director can exercise his voting rights at a general meeting in favour of a contract in which he is interested.

*Example:* Company Y with a paid-up capital of ₹ 50 lakhs entered into a contract with company Z which has paid up capital of ₹ 5 lakhs. A director of a company Y is holding equity shares of the nominal value of ₹ 50,000 in Z company. The director does not disclose his interest at the board meeting under s. 299. The holding of the director is less than two percent of ₹ 5 lakhs. Therefore, the director is not liable to disclose his interest under s. 299(6).

## 10.9 Service Contract

### Directors not to Hold Office or Place of Profit

Section 314 imposes certain restrictions on the holding of office or place of profit in a company by the directors and their associates. Following is the summary of restrictions so provided:

1. ***Section 314 (1) (a):*** No director of a company shall hold any office or place of profit (carrying any remuneration) under the company or its subsidiary except with the consent of the company by a special resolution. It shall, however, be sufficient if the special resolution is passed at the first general meeting held after such appointment.
2. ***Section 314 (1) (b):*** Except by passing a special resolution, and the approval of the central government the following persons shall not hold any office or place of profit carrying a total monthly remuneration of such sum as may be prescribed (presently ₹ 10,000 per month):
   - A partner or relative of a director or manager;
   - A firm in which such director or manager, or relative of either, is a partner;
   - A private company of which such a director or manager, or relative of either, is a director or member.

   Again, special resolution may be passed at the first general meeting after the appointment made. Where, however, the aforesaid appointment is made without the knowledge of the director, the consent of the company may be obtained either in the general meeting aforesaid or within three months from the date of the appointment, whichever is later.

   However, a director or any of his associates may be appointed as managing director, manager, banker or trustee for the debenture-holders of the company without sanction of special resolution, if the remuneration received from such subsidiary in respect of such office or place of profit is paid over to the company or its holding company.

Notes

For the aforesaid appointment of a director or his associates, special resolution shall not only be necessary at the time of first appointment but also for every subsequent appointment on a higher remuneration not covered by the special resolution except where an appointment on a time-scale has already been approved by the special resolution.

It may be noted that the aforesaid restrictions do not apply where a relative of a director or a firm in which such relative is a partner holds any office or place of profit under the company or a subsidiary thereof having been appointed to such office or place before such director became a director of this company [s. 314(1A)].

3. ***Section 314(1)(B):*** (i) no partner or relative of a director or manager; (ii) no firm in which such director or manager, or relative of either is a partner; (iii) no private company of which such a director or manager, or relative of either, is a director or member, shall hold an office or place of profit in the company carrying a total monthly remuneration of not less than such sum as may be prescribed (presently, ₹ 50,000 per month) except by passing a special resolution and the approval of the Central Government.

4. ***Section 314(2)(C):*** If any director or his associate holds an office or place of profit in contravention of the aforesaid provisions, then: (i) he shall be deemed to have vacated such office or place of profits as such on and from the date next following the date of the general meeting; (ii) he shall be liable to refund to the company any remuneration received or the monetary equivalent of the perquisites or advantage enjoyed by him. The company cannot waive the recovery of any sum refundable to it as above unless, permitted to do so by the Central Government.

These provisions will neither affect the director's office as such nor shall he be liable to refund remuneration received in the capacity of a director, e.g; if some commission or monthly remuneration is payable to all the directors, the same will not be refundable, but if a director receives something in addition to other directors that he will be bound to pay to the company. Thus, for the purposes of this section, an office and place of profit is to be deemed to be one of profit if in case it is held by a director, such director over and above his remuneration as a director, and in case it is held by any other person, firm or private company or a body corporate, obtains anything from the company by way of remuneration, whether as salary, fees, commission, or perquisites, right to occupy any premises rent-free as a place of residence or otherwise.

Section 629 (A) also provides for a fine of ₹ 5,000 and a further fine of ₹ 500 for every day during the period in which contravention continues.

Section 314 (2A) makes it obligatory for every individual, firm, private company, or other body corporate proposed to be appointed to any office or place of profit to which this section applies to declare in writing before or at the time of appointment, whether he or it is or is not connected with any director of the company in any of the ways referred to in s.314 (1).

The aforesaid restrictions do not apply to a person who being the holder of any office of profit in the company is appointed by the Central Government, under s.408, as a director of the company. [s. 314(4)].

## 10.10 Removal of Directors

A director may be removed by:

1. Shareholders
2. Central Government
3. CLB

Notes

### 10.10.1 Removal by Shareholders

Section 284 provides that a company may, by ordinary resolution passed in general meeting after special notice, remove a director before the expiry of his term of office. On receipt of the special notice, the company must forthwith send a copy thereof to the director concerned to enable him to make a representation. If he makes a representation in writing and requests the company to notify it to the members, the company must, unless it is received by it too late for it to send to the members, state the fact of the representation in any notice of the resolution given to the members. It should also send a copy of the representation to every member of the company to whom notice of the meeting is sent. If the representation is not sent as aforesaid, the company must at the instance of the director concerned read it out at the meeting. The director is also entitled to be heard on the resolution at the meeting.

The special notice given by the member(s) must specify the reasons for removal of the director.

However, the copy of the representation of the director sought to be removed, need not be circulated nor the concerned director be allowed the right to have the representation read out in the general meeting (where the same was not circulated earlier because of late receipt), if the company or any other person claiming to be aggrieved, has made an application to CLB to prevent such circulation or reading out on the ground that such circulation or reading out would amount to abuse of the right on the part of the concerned director to secure needless publicity for defamatory matters, and CLB, being satisfied, orders accordingly.

The vacancy caused by the removal of a director may be filled at the same meeting and if so filled, the person appointed thereto will only hold office for the residual period of the removed director. If the vacancy is not filled by the company in general meeting, the Board of directors may fill it as if it were a casual vacancy in accordance with s.262, but the board cannot appoint the removed director.

A removed director may claim compensation for loss of office as a director, or claim damages for the termination of any other office on account of the removal, or may continue to hold the additional office.

But the following directors cannot be removed by the company in general meeting:

- A director appointed by the Central Government under s.408.
- A director of a private company holding office for life on April 1, 1952.
- A director elected by the principle of proportional representation under s.265.
- A director appointed by the Central Government under Industries (Development and Regulation) Act, 1951.
- A director appointed under Sick Industrial Companies (Special Provisions) Act, 1985.
- A director appointed by financial institutions under their statutory powers.
- A nominee director.
- A director appointed by CLB (s. 402).

It is to be noted that s.284 is not exhaustive as it is stated therein that nothing in s.284 shall be taken as derogating from any power to remove a director which may exist apart from the section. The articles of a company may provide for the removal of a director.

Thus it is to be noted that the power to remove a director is not an absolute or unrestricted one.

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*Example:* The shareholders of X Co. Ltd. sought to remove a director at a meeting. The concerned director alleged that this could not be done as no special notice was given to pass a resolution to remove him. As such he was deprived of his right to make a representation. The shareholders' contention that the sending of the special notice and the right of the director to make a representation were only a formality was not tenable. [Queen Kuries and Loans (P) Ltd. v. Sheena Jose, (1993) 76 Comp. Cas 821 Ker]. The contention of the director was held to be correct.

*Example:* If in the above example, one shareholder holding ten equity shares of ₹ 10 each fully paid up had given a special notice for the removal of the director, but did not state any reasons for the removal. Even in such a case, the director cannot be removed, as the disclosure of the ground for removal is a matter of substance and not of form because the director concerned is entitled to make a representation in writing against his removal. How can he make the representation, if he does not know the reasons of his removal.

### 10.10.2 Removal by the Central Government

The provisions of s. 203 and s. 204 prohibit certain persons from acting or being appointed as directors, and provide for their removal only if they were convicted for offences involving moral turpitude. In all those cases, conviction or finding of guilt by the court is the prerequisite for bringing about vacation of office. Strict proof of guilt in a criminal case is essential and very often such persons may go scot-free in spite of malpractices. The findings of the CLB will enable the Central Government to take quick action against persons involved in cases of fraud, etc. For this purpose, s.388B to 388E have been inserted in the Act.

Under s.388B, the Central Government has the power to make a reference to the CLB against any managerial personnel. The power can be exercised where, in the opinion of the Central Government, there are circumstances suggesting:

1. At the personal level, that any person concerned in the conduct and management of the affairs of a company is or has been guilty of fraud, misfeasance, persistent negligence of default in carrying out his obligations and functions under the law, or breach of trust in connection therewith; or
2. At the company level. that the business of the company is not or has not been conducted and managed by such person in accordance with sound business principles or prudent commercial practices; or
3. At the industry level, that the business of the company is or has been conducted or managed by such person in a manner which is likely to cause or has in fact caused, serious injury or damage to the interest of trade, industry or business to which such company pertains; or
4. At the community level, that the business of the company is or has been conducted and managed by such person with an intent to defraud its creditors, members, or any other person or otherwise for a fraudulent or unlawful purpose or in a manner prejudicial to public interest.

The reference may be made by stating a case against the person aforesaid, with a request that, the CLB may inquire into the case, record finding as to whether or not such person is a fit and proper person to hold the office of director or any other office connected with the conduct and management of any company.

The statement of the case by the Central Government should be in the form of an application presented to the CLB and the person against whom such case is stated and referred should be

Notes

joined as a respondent to the application. The application should contain a concise statement of such circumstances and materials as the Central Government may consider necessary for purpose of inquiry to be made by the CLB. The application must be signed and verified in the same manner as a complaint in a suit by the Central Government under the Code of Civil Procedure.

Thereafter, the CLB will hear the case against the respondent. At any stage of the proceedings, the CLB may allow the Central Government to alter or amend the application in such a manner and on such terms as may be just and all such alterations and amendments shall be made as may be necessary for the purpose of determining the real question in the inquiry (s.388B).

If during the pendency of the case the CLB finds it necessary, in the interest of the members or creditors of the company, it may, either on the application of the Central Government or of its own motion, direct that the respondent shall not discharge any of the duties of his office until further orders and appoint in his place another suitable person to discharge the duties of the respondent. This person, who is temporarily appointed to discharge the duties in place of the respondent will be regarded as a public servant within the meaning of s.21 of the Indian Penal Code (s.388C).

At the conclusion of the hearing of the case, the CLB shall record its findings, stating therein specifically as to whether or not respondent is a fit and proper person to hold the office of director or any other office connected with the conduct and management of any company (s.388-D).

On the basis of the aforesaid findings, the Central Government may, by order, notwithstanding any other provisions contained in the Act, remove the delinquent respondent from his office (s.388E(1)).

An order under s.388E must not be passed against any person unless he has been given a reasonable opportunity to show cause against the order. However, no matter can be raised by such a person before the Central Government, which has already been decided by the CLB (s.388E(2) and proviso thereto).

After the delinquent person has been, by order, removed, he shall neither hold any office for a period of 5 years from the date of the order of removal nor will he be paid any compensation for loss of office as a result of removal. The time-limit may, however, be relaxed by the Central Government with the previous concurrence of the CLB, and the Central Government may accordingly permit such person to hold the office of a director or any other office connected with the conduct and management of the affairs of the company even before the expiry of the period of 5 years. On the removal of the person, the company may, with previous approval of the Central Government, appoint another person to that office in accordance with the provisions of the Act.

### 10.10.3 Removal by Company Law Board

Section 402(b) empowers the CLB to remove some managerial personnel when an application to it is made for prevention of oppression and mismanagement under Ss. 397 and 398. Under this section, if the CLB finds that, the relief ought to be granted, it may terminate, set aside or modify any agreement between the company and the managing director or any other director or the manager. When appointment of a managerial personnel is so terminated or set aside, he can neither sue the company for damages or compensation for the loss of office, nor can he be appointed, except with the leave of the CLB, in any managerial capacity in the company for a period of 5 years from the date of the order terminating or setting aside his contract with the company. Also the removed director shall not be entitled to claim any compensation from the company for loss of his office.

Notes

A Director of a private company is appointed as its managing director on a monthly salary of ₹ 10,000. There is an objection to this on the ground that a director cannot be appointed to an office of profit. Advise.

## 10.11 Retirement of Director

The directors due to retire by rotation vacate office at the latest on the last day on which an annual general meeting could have been held under s. 166, and therefore, if this meeting is not held, the directors cannot claim to continue after the date on which the meeting should have been held. The reasons for not allowing directors to continue after the date on which the AGM should have been held is that as it is the duty of the directors to call the AGM within the prescribed time, they cannot be allowed to take advantage of their own default and by that means to continue in office for the extended period [B.R. Kundra v. Motion Pictures Assn. (1976) 46 Comp Cas. 339 Del].

## 10.12 Appointment of a Director other than a Retiring Director

Section 257 provides for the procedure of appointment of a person other than the retiring director. If any person, (whether a member of the company or not) other than the retiring director wishes to stand for directorship, he must signify his intention to do so by giving 14 days' notice to the company before the meeting and the company must inform the members not later than seven days before the meeting either by individual notices or by advertisement of this fact in at least two newspapers circulating in the place where its registered office is situated, of which one must be in English and the other in the regional language of the place. Also, the candidate or the member who intends to propose him as director has to deposit a sum or ₹ 500 which shall be refunded to such person or as the case may be, to such other member, if the candidate succeeds in being elected. In case such person is not elected as director, he or the member, as the case may be, will not be entitled to the refund of ₹ 500 and the amount deposited shall stand forfeited to the company. Also s.264 requires every person proposed as a candidate for the office of a director to sign and file first with the company his consent to act as a director, if appointed and then with registrar within 30 days of his appointment.

*Example:* The BOD of XYZ Ltd. appoints Mr. A as a director in the vacancy caused by resignation of Mr. B. Now at the ensuing AGM, Mr. A is to vacate his office. The company is contemplating to reappoint him as a director, treating him as a retiring director.

The company cannot treat A as a retiring director under s. 257. Therefore, he cannot be deemed to have been reappointed. The procedure given in s. 257 will have to be followed for his appointment.

## 10.13 Power and Fiduciary Duties

### 10.13.1 Powers of the Board of Directors

Section 291 provides for general powers of the Board of directors.

"Subject to the provisions of the Act, the Board of directors of a company shall be entitled to exercise all such powers and to do all such acts and things, as the company is authorised to exercise and do"

Notes

However, the Board cannot exercise any power or do any act or thing which is directed or required, whether by this or any other Act or by the memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting. In exercising any such power or doing any such act or thing, the board will be subject to the provisions contained in that behalf in this or any other Act, or in the memorandum or articles of the company, or in any regulations not inconsistent therewith and duly made thereunder, including regulations made by the company in general meeting.

Thus, the Board may exercise all powers of the company and can do all such acts and things that the company can do. But the exercise of such powers of the Board shall be in conformity with the provisions of the Companies Act or any other Act and memorandum, articles and resolutions of the company in general meetings. Thus, a general meeting may, by amending the articles, restrict the powers of the board. But the meeting cannot invalidate any act validly done by the board except in the following cases: (1) where the directors are either unable or unwilling to act [Barron vs. Potter (1914) 1 Ch. 895]; (2) when the directors act for their own personal interests in complete disregard to the company [Marshall's Value Gear Co. Ltd. vs. Manning Wardle & Co. Ltd (1909) Ch. 267]; (3) when the Board has become incompetent to act e.g. where all the directors constituting the Board are interested in a dealing or where none of the directors was validly appointed [B.N. Vishwanathan vs. Tiffins B.A. and Ltd. AIR (1953) Mad 510].

### 10.13.2 The Mode or Manner of Exercise of Board's Powers

Section 292 provides that the Board of directors of a company shall exercise the following powers on behalf of the company and it shall do so only by means of resolutions passed at meeting of the Board:

(i) The power to make calls on shareholders in respect of money unpaid on their shares;

(ii) The power to buyback its shares under s. 77A;

(iii) The power to issue debentures;

(iv) The power to borrow money otherwise than on debentures;

(v) The power to invest funds of the company (subject to sections 293 and 372A); and

(vi) The power to make loans. (subject to sections 293 and 372 A).

The Board may, however, by a resolution passed at a meeting delegate to any committee of directors, the managing director, the manager or any other principal officer of the company, the powers specified in clauses (iv), (v) and (vi) on such conditions as the Board may prescribe.

Besides the powers specified in s.292, there are certain other powers also which can be exercised only at the meeting of the Board. These are:

1. The power of filling casual vacancies in the Board (s.262);
2. Sanctioning of a contract in which a director is interested [s.297];
3. The power to recommend the rate of dividend to be declared by the company at the Annual General Meeting, subject to the approval by the shareholders.

In the following cases, not only that the powers be exercised at the Board's meeting but also that every director present and entitled to vote must consent thereto:

1. The power to appoint a person as managing director or manager, who is already managing director or manager of another company (Ss.316 and 386).
2. The power to invest in any shares and debentures of any other body corporate (s.372).

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### 10.13.3 Restrictions on Powers of Directors

Section 293 provides that, the Board of directors of a public company or a private company which is a subsidiary of a public company cannot exercise the following powers without the consent of the shareholders in general meeting:

1. Sell, lease or otherwise dispose of the whole, substantially the whole, of the undertaking of the company, or where the company owns more than one undertaking, of the whole or substantially the whole, of any such undertaking.

   However, this restriction does not apply to the case of a company whose ordinary business is to sell or lease property.

2. Remit or give time for the re-payment of any debt due by a director except in the case of renewal or of continuance of an advance made by a banking company to its director in the ordinary course of business.

3. Invest, otherwise than in trust securities, the amount of compensation received by the company in respect of compulsory acquisition of any fixed assets of the company.

4. Borrow money exceeding the aggregate of the paid-up capital of the company and its free reserves. 'Borrowing' does not include temporary loans obtained from the company's bankers in the ordinary course of business.

   The expression 'free reserves' mean reserves not set apart for any specific purpose.

   Further, every resolution passed by the company in general meeting shall specify the total amount up to which moneys may be borrowed by the board. Furthermore, the expression 'temporary loans' means loans repayable on demand or within six months from the date of the loan such as short term, cash credit arrangement, the discounting of bills and the issue of other short term loans of a seasonal character, but does not include loans raised for the purpose of financing expenditure of a capital nature.

5. Contribute in any year, to charitable and other funds not directly relating to the business of the company or the welfare of its employees, any amount exceeding ₹ 50,000 or 5% of its average net profit for the last three financial years, whichever is greater.

However, contributions to National Defence Fund or any other fund approved by the Central Government for the purpose of national defence are exempted from the above provisions. Any amount may be contributed without obtaining the sanction of the company in general meeting. However, the amount contributed to these funds must be disclosed in the profit and loss account of the company for the year in which the contribution was made.

The Companies Act does not expressly empower companies to borrow money. Therefore, most of the companies expressly provide for such borrowing powers in the memorandum. In such a case, where memorandum authorises the company to borrow, the articles provide as to how and by whom these powers shall be exercised. It may also fix up the maximum which can be borrowed by the company.

*Example:* The paid up share capital and free reserves of XYZ Ltd. is ₹ 100 crore as on April 1, 2008. The shareholders of the company at their general meeting held on April 4, 2008, by a resolution authorised the board of the company to borrow money 'exceeding the paid-up share capital and free reserves of the company, to the extent required by the board of directors." The board, as a result, borrowed money to the extent of ₹ 130 crore, including ₹ 20 crore as short term loan and ₹ 25 crore as a temporary loan for financing the construction of a building of the company.

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The borrowing made by the board violates the provisions of the Act because (i) it exceeds the paid up capital and free reserves even after excluding short term loan of ₹ 20 crore assuming that the loan is obtained from the companies bankers in the ordinary course of business. (ii) the resolution passed in the general meeting enabling the board to borrow in excess of its paid up capital and free reserves without specifying the total amount up to which money may be borrowed by the board.

*Example:* The position would be different in case the company's paid up share capital and free reserves increased to ₹ 150 crore and the board borrow money to the extent of ₹ 140 crore which neither include any short-term loan nor temporary loan for financing of the construction of a building for the company. As the board could raise up to ₹ 150 crores, but in fact has raised ₹ 140 crore only, there is no contravention of the provision of the Act.

### Self Assessment

8. Minimum no. of Directors in case of a public company is

   (a) 1 (b) 2

   (c) 3 (d) 4

9. Minimum no. of Directors in case of private company is

   (a) 1 (b) 2

   (c) 3 (d) 4

10. Age limit of Directors in case of public company is

    (a) 65 (b) 70

    (c) 60 (d) 55

11. Age limit of Directors in case of private company is

    (a) 65 (b) 70

    (c) 75 (d) No limit

## 10.14 Duties of Director in Relation to Good Corporate Governance

Duties of directors may be divided under two heads: (1) Statutory duties; and (2) Duties of a general nature. The statutory duties are the duties and obligations imposed by the Companies Act. These have been discussed at appropriate places. Important among them are:

1. ***To file Return of Allotments:*** Section 75 charges a company to file with the Registrar, within a period of 30 days, a return of the allotments stating the specified particulars. Failure to file such return shall make directors liable as 'officer in default'. A fine up to ₹ 500 per day till the default continues may be levied.

2. ***Not to Issue Irredeemable Preferences Shares or Shares Redeemable after 10 years:*** Section 80 forbids a company to issue irredeemable preference shares or preference shares redeemable beyond 10 years. Directors making any such issue may be held liable as 'officer in default' and may be subject to fine up to ₹ 1,000.

3. ***To Disclose Interest [Ss.299-300]:*** A director who is interested in a transaction of the company must disclose his interest to the Board. The disclosure must be made at the first meeting of the Board held after he has become interested. This is because a director stands

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in a fiduciary capacity with the company and therefore, he must not place himself in a position in which his personal interest conflicts with his duty. Interest should be such which avoids conflicts with the duties of the director towards the company.

Notice, however, that the Companies Act does not debar a company from entering into a contract in which a director is interested. It only requires that such interest be disclosed. An interested director should not take part in the discussion on the matter of his interest. His presence shall not be counted for the purpose of quorum. He shall not vote on that matter. If he does vote, his vote shall be void. Non-disclosure of interest makes the contract voidable and not void. Where the whole Board of directors is aware of the facts, a formal disclosure is not necessary (Venkatachalapathi vs. Guntur Mills AIR 1929 Mad 353). In this case, a loan was advanced by the wife of a director creating a mortgage on the property of the company. The director did not disclose his interest and he even voted on the matter. The company later sued to have mortgage set aside.

***Held***: the fact was known to all directors and a formal disclosure was not necessary. As regards voting by the interested director, it was held that the voting would not render the contract void or voidable unless in the absence of that vote, there would have been no quorum qualified to contract.

4. ***To disclose receipt from transferee of property:*** Section 319 provides that any money received by the directors from the transferee in connection with the transfer of the company's property or undertaking must be disclosed to the members of the company and approved by the company in general meeting. Otherwise the amount shall be held by the directors in trust for the company. This money may be in the name of compensation for loss of office but in essence may be on account of transfer of control of the company. But if it is bona fide payment of damages for a breach of contract, then it is protected by s.321(3).

5. ***To disclose receipt of compensation from transferee of shares:*** If the loss of office results from the transfer (under certain conditions) of all of the shares of the company, its directors would not receive any compensation from the transferee unless the same has been approved by the company in general meeting before the transfer takes place (s.320). If the approval is not sought or the proposal is not approved, any money received by the directors shall be held in a trust for the shareholders who have sold their shares.

Section 320 further provides that in pursuance of any agreement relating to any of the above transfers, if the directors receive any payment from the transferee within one year before or within 2 years after the transfer, it shall be accounted for to the company unless the director proves that it is not by way of compensation for loss of office.

Section 321 further provides that, if the price paid to a retiring director for his shares in the company is in excess of the price paid to other shareholders or any other valuable consideration has been given to him, it shall also be regarded as compensation and should be disclosed to the shareholders.

Some other statutory duties are: to attend the Board meetings; to convene and hold general meetings; to prepare and place before AGM financial accounts; to make declaration of solvency.

The general duties of directors are as follows:

1. ***Duty of good faith:*** The directors must act in the best interest of the company. Interest of the company implies the interests of present and future members of the company on the footing that the company would be continued as a going concern.

   A director should not make any secret profits. He should also not exploit to his own use the corporate opportunities. In Cook vs. Deeks (1916) AC 554, it was observed that "Men who assume complete control of a company's business must remember that they are not

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at liberty to sacrifice the interest which they are bound to protect and while ostensibly acting for the company, direct in their own favour business which should properly belong to the company they represent." In this case, there was an offer of a contract to the company. Directors who were the holders of shares of 3/4 of the votes resolved that the company had no interest in the contract and later entered the contract by themselves.

***Held:*** The benefit of the contract belonged in equity to the company.

2. ***Duty of Care:*** A director must display care in performance of the work assigned to him. He is, however, not expected to display an extraordinary care but that much care only which an ordinary prudent man would take in his own case. Justice Romer in Re City Equitable Fire Insurance Company [1925 Ch. 407] observed, "His (director's) duties will depend upon the nature of the company's business, the manner in which the work of the company is distributed between the directors and other officials of the company. In discharging these duties a director must exercise some degree of skill and diligence. But he does not owe to his company the duty to take all possible care or to act with best care. Indeed, he need not exhibit in the performance of his duties a greater degree of skill than may reasonably be expected from a person of his knowledge and experience. It is, therefore, perhaps, another way of stating the same proposition that directors are not liable for mere errors of judgement."

   Similar view was expressed in Langunas Nitrate Co. vs. Lagunas Nitrate Syndicate (1899) 2 Chi. 392, in the following words: "If directors act within their powers, if they act with such care as is to be reasonably expected of them having regard to their knowledge and experience and if they act honestly for the benefit of the company they discharge both their equitable as well as legal duty to the company."

   Section 201 states that, a provision in the company's articles or in any agreement that excludes the liability of the directors for negligence, default, misfeasance, breach of duty or breach of trust, is void. The company cannot even indemnify the directors against such liability. But if a director has been acquitted from such charges, the company may indemnify him against costs incurred in defense. Section 633 further states that, where a director may be liable in respect of the negligence, default, breach of duty, misfeasance or breach of trust but if he has acted honestly and reasonably and having regard to all the circumstances of the case, he ought fairly to be excused, the court may relieve him either wholly or partly from his liability on such terms as it may think fit.

3. ***Duty to attend Board Meetings:*** A number of powers of the company are exercised by the Board of directors in their meetings held from time to time. Although a director is not expected to attend all the meetings but if he fails to attend three consecutive meetings or all meetings for a period of three months, whichever is longer, without permission, his office shall automatically fall vacant.

4. ***Duty not to Delegate:*** Director, being an agent, is bound by maxim 'delegatus non protest delegare' which means a delegate cannot further delegate. Thus, a director must perform his functions personally. A director may, however, delegate in the following cases: (a) where permitted by the Companies Act or articles of the company; (b) having regard to the exigencies of business certain functions may be delegated to other officials of the company.

Some other duties are to convene statutory; annual general meeting and also extraordinary general meeting when required by the shareholders of the company; to prepare and place at the AGM along with the balance sheet and profit and loss account, a report on the company's affairs; to make a declaration of solvency in the case of a member's voluntary winding up.

# COMMITTEES

***Committees are a sub-set of the board, deriving their authority from the powers delegated to them by the board.***
Under Section 177 of **Companies Act, 2013**, Board of Directors may delegate certain matters to the committees set up for the purpose. Committees are formed as a means to improve board effectiveness and efficiency in areas where more focused, specialised and technically oriented discussions is required.

***Following are some of the important committees to be constituted by the Board:***

***1. Audit Committee:***

***Applicability:***

- Every Listed Public Companies and Public Companies having a Paid-up share capital of 10 crore rupees or more, and a turnover of Rs. 100 Crore or more.
- Additionally All Public Companies which have in aggregate outstanding loans, debentures and deposits exceeding 50 crore rupees are required to constitute an Audit Committee.

***Composition of Audit Committee as per Companies Act, 2013:***

- Minimum 3 directors with majority of Independent Director.
- Members including the Chairman of Audit Committee should be able to read and understand financial statement.

***Composition of Audit Committee as per clause 49 of Listing Agreement:***

- Minimum of 3 Director of which 2/3rd are independent Directors.
- All members should be financially literate and at least 1 member shall have accounting or related financial management expertise.

**Vigil Mechanism:**

Vigil Mechanism provides adequate safeguard against victimisation of persons. It is established for directors and employees to report their grievances and concerns.

Rule 7 of Companies (Meetings of Board and its Powers) Rules, 2014 describes about establishment of Vigil

Mechanism for every Listed Company and companies prescribed below:

- Companies which accepts deposits from public.
- Companies which have borrowed money from bank and public financial institutions in excess of Rs.50 Crores.
- The Board of Directors shall nominate a director to play role of Audit Committee for the purpose of Vigil Mechanism for reporting purpose. The aggrieved person will have direct access with the Chairperson/Nominated Director of the Audit Committee.

- The details of establishment of such mechanism shall be disclosed on the company's website, and in the Board 'report.

**Penalty for the Violation of Audit Committee Provisions:**

The Company shall be punishable with a fine of Rs. 1 lakh to Rs. 5lakh and every officer of the company who is in default shall be punishable with imprisonment upto 1 year or with Rs. 25,000 to Rs. 1 lakh or with both.

***Function of Audit Committee:***

- To recommend appointment, remuneration and terms of appointment of the Auditor of the Company.
- To establish a Vigil Mechanism Policy.
- To call for remarks of the auditors about the internal control system.
- At the Annual General Meeting, the chairman of the Committee should be present to answer the shareholder's inquiry.
- To discuss any issues related to internal and statutory auditors and the management of the Company.

***2. Nomination and Remuneration Committee:***

***Applicability:***

- Every Listed Public Companies and Public Companies having a Paid-up share capital of 10 crore rupees or more, and a turnover of Rs. 100 Crore or more.
- Additionally All Public Companies which have in aggregate outstanding loans, debentures and deposits exceeding 50 crore rupees are required to constitute an Audit Committee.

***Composition of Nomination and Remuneration Committee as per Companies Act,2013:***

- Minimum of 3 Non-Executive Directors out of which two shall be Independent Directors.
- Chairperson shall be an Independent director.

***Functions of Nomination and Remuneration Committee:***

- Recommendation of success plans for the directors.
- To review the elements of the remuneration package, structure of remuneration package.
- To review the changes to remuneration package, terms of appointment, severance fee, requirement and termination policies and procedures.
- To recommend the shortlisted candidates who are qualified to be director and who can be appointment in senior management.
- The committee is authorised to seek information about any employee and the management is directed to co-operate.
- The Committee can be present at the General Meeting to answer the shareholder's queries.

***3. Stakeholders Relationship Committee:***

Section 178 of Companies Act,2013 states that a company which holds 1000 numbers of shareholders, debenture holders, deposit holders and any other security holders at any time during a financial year.

***Composition of Stakeholders Relationship Committee:***

- As per the SEBI Listing regulations the Committee should consist of least three directors, with at least one being an Independent director, shall be members of the committee and in case of a listed entity having outstanding SR equity shares, at least two-thirds of the committee shall comprise of independent directors.
- The chairperson of the Committee shall be a non-executive director and such other members as may be decided by the Board.
- As per regulation the Committee shall meet at least once in a year. The chairperson or, in his absence any other member of the committee authorized by him in this behalf shall attend the general meetings of the Company.

***Functions of Corporate Stakeholders Relationship Committee:***

The Committee shall resolve complaints related to transfer/transmission of shares, non-receipt of annual report and non-receipt of declared dividends, general meetings, approve issue of new/ duplicate certificates and new certificate on split/consolidation/ renewal etc. approve transfer/transmission, dematerialization.

***4. Corporate Social Responsibility Committee:***

Section 135 of Companies Act,2013 , with Companies(CSR Policy) Rules,2014 states that every company having :

- net worth of not less than Rs.500 crores or more
- or turnover of not less than Rs. 1000 crores or more
- Or Net Profit of Rs.5crore or more shall constitute a Corporate Social Responsibility Committee.

***Composition of CSR Committee as per Companies Act, 2013 :***
In case of Listed Company at least 3 Directors out of which 1 should be an Independent Director.

***Functions of Corporate Social Responsibility Committee:***

- To suggest and devise a CSR Policy according to the Schedule VII of Companies Act, 2013 to the board.
- To recommend the amount of expenditure of the devised policy above.
- To monitor the CSR Policy of company from time to time and prepare a transparent monitoring mechanism.
- Institution of a transparent monitoring mechanism for implementation of the CSR projects or programs or activities undertaken by the company.

# INSIDER TRADING

"An act of trading, directly or indirectly, in the securities of a publicly listed company by any person, who may or may not be managing the affairs of such company, based on certain information, not available to the public at large, that can influence the market price of the securities of such company."[1]

## LEGAL REGIME

The first country to make a law against insider trading was America.[2] In India, the first effort to address this problem was made in 1947 by the establishment of the Thomas Committee.[3] The recommendations of the committee were later codified under various provisions of The Companies Act, 1956. Soon with evolution of the corporate sector came in the establishment of Securities and Exchange Board of India (SEBI) in 1988. In 1992 came in the SEBI Act along with SEBI (Prohibition of Insider Trading) Regulations, 1992[4]. This led to a statutory evolution against the practice of insider trading in India.
The laws kept on becoming stricter and tighter with time in order to cover every loophole available. In 2015 came in a major development when the SEBI brought in SEBI (Prohibition of Insider Trading) Regulations, 2015[5]which replaced the older regulations of 1992 and addressed most of the problems of the older regulation. In 2018, SEBI formed a committee under the Chairmanship of T.K. Viswanathan[6] to take a deeper look into the problems of the new regulations and give its recommendations. On receiving the Committee's report [7], SEBI made the latest amendments to these regulations in 2019 which are now the present laws against insider trading in India.

## PROHIBITION AND EXCEPTIONS TO INSIDER TRADING IN INDIA

The relevant provisions which govern insider trading in India are Section 195[8] of the **Companies Act, 2013** along with section 12A[9] and 15G[10] of the SEBI Act, 1992. In addition to these provisions the primary regulations which govern insider trading in India are the SEBI (Prohibition of Insider Trading) Regulations, 2015. The prohibition and exception/defenses to insider trading can be found in the SEBI (Prohibition of Insider Trading) Regulations, 2015.

Section 12A(d) of the SEBI Act.1992 expressly prohibits insider trading[11] while section 15G imposes a penalty of a sum ranging between ten lakhs to twenty-five crore rupees or a penalty of a sum which is three times the amount of profit made, whichever is higher[12]. Section 195 of the Companies Act, 2013 too prohibits insider trading in addition to defining what it is and states that a punishment of five years of imprisonment and/or a fine up to rupees twenty-five crores maybe imposed on the defaulter.

Regulation 3(1) of the **SEBI (Prohibition of Insider Trading) Regulations, 2015**[13] lays down the first prohibition on insider trading and states that no insider shall communicate any UPSI relating to a company to any person. The term 'any person' also included other insider of the company as well. Hence, it states that a person who is in possession of UPSI shall neither communicate such UPSI to outsiders nor insiders. However, it also carves an exception and states that such disclosure of information maybe be allowed in cases where such communication is made for legitimate purposes, performance of duties or discharge of legal obligations. On the recommendation of the T.S. Viswanathan

committee, a few examples of legitimate expectations were added wherein such disclosure in ordinary course of business to partners, collaborators, etc. would fall under the exception. However, under regulation 2B it also states that any such person to whom the UPSI is disclosed to for legitimate purpose like lawyers, accountants, partners, etc. from that point will fall under the definition of insider and hence all the prohibition of the regulation would also apply to them too. This concept can be seen to have been borrowed from the US concept of "constructive insiders" as laid down in the case of Dirks v. SEC [14]. This case stated that any such person like lawyers, accountants, etc. who are actually outsider will be construed as insiders from the point at which the UPSI was shared with them under ordinary course of business.

Another exception to this prohibition is carved out in sub-regulation 3 of regulation 3[15] wherein such UPSI is permitted to be disclosed or allowed access to in two circumstances. **Firstly,** in cases where due to the takeover regulations, obligations to make an open offer arise and the BoD is of informed opinion that doing so would be in the best interest of the company. Secondly, in a case where no obligations arise however the BoD feels that disclosing such information would be in the best interest of the company. In the second case, the UPSI about a transaction should be made public atleast two days prior to the said transaction takes place. The important thing to note here is that in both such cases the disclosure has to be made to the entire public and not a selective group.
What this does it that it gives every person an equal opportunity to make full use of such information and eliminates the possibility of a few people benefitting from the information. Hence it purports to the motive of the regulation which was to avoid unlawful gain by a few.

An important point regarding this prohibition was highlighted by SAT in its judgement of Samir Arora v. SEBI [16]. Here, Samir Arora was accused of disclosing certain UPSI about a merger and eventually making a profit for himself. However, it was later found that the information disclosed by him was false or uncertain as at the day of disclosure no such merger decision had taken place. SAT ruled that since the information was false the prohibition of non-disclosure won't be attracted as the information has to be true to constitute a UPSI and to attract a charge of insider trading [17].

The **second** prohibition against insider trading is laid down under regulation 3 sub-regulation 2[18] which prohibits any person i.e. insider or outsider from procuring any UPSI related to a company. This prohibition goes in tandem with the first prohibition and restricts any person from getting access to UPSI regarding a company. The same exception of "legitimate purpose" has been carved out in this provision as well.

The **third** and the most important exception is laid down in regulation 4[19] which prohibits any person in possession of UPSI of a listed company from trading in securities of that company on the stock market [20]. It was held by SAT in Chandrakala v. SEBI [21] that if an insider deals in securities while in possession of UPSI then it would be presumed that he traded on the basis of such UPSI[22]. However, **six exceptions** have been carved out to tis prohibition in regulation 4.

**Firstly**, an exception has been made for an off-market inter-se transaction. These are transactions between two people who are both 'insiders' and possess the same UPSI and

have taken a conscious decision to trade. Since both parties possess the same UPSI, there would be no unlawful gain to either as both of them have agreed to the transaction on the basis of same information i.e. UPSI. **Secondly**, the block deal window mechanism falls under the exception. However, such block deals should again take place between two persons who both have the same UPSI as this would remove the risk of unlawful gains. **Third** is the exception wherein the trading took place under statutory of regulatory obligations. Hence, when such trading was forced by legal requirements then the prohibition would not apply. The **fourth** exception allows transaction which are in furtherance of stock options. Hence, when the purchase price is pre- determined than such a prohibition on trading would not apply. This exception however leaves some room for misuse and hence needs to be relooked. **Fifth** exception applies to non-individual insiders and states that when a group of insiders (where some possess UPSI) deal together, it should be proved that the insiders who actually took the trading decisions were not in possession of UPSI and were different entities from those possessing such UPSI. **Lastly**, an exception is created for trades conducted on the basis of trading plan.

Trading plan is an instrument which helps the people, who are continuously in possession of UPSI due to the nature of their job, to trade in securities. It is an instrument whereby such people can plan for trades in future. What this does is that it creates a certain time lag between the trading decision and its execution due to which the UPSI which the person might possess while deciding would become publicly available and hence not lead to an unlawful gain by such person. According to regulation 5[23] such trading plan needs to be presented atleast six months prior to the execution of such proposed transaction. It is important to note that only the number of securities is decided in a plan and the price of such securities would be the price as listed on the stock market on the day of execution of the plan. Hence, in those six months, all the UPSI would be public and won't lead to an unfair gain by the person. Also, such plan shall entail trading for a period of at least twelve months and shall have to be approved by a compliance officer who will then make a public disclosure of such plan. Such plan should also not overlap an existing trading plan and nor shall entail any such transaction which shall lead to market abuse. It is also important to note that under regulation5 (4), the trading plan has been made an irrevocable instrument and once approved it has to be mandatorily enforced by the person irrespective of monetary nature i.e. profit or loss on the day of execution.

However, if the UPSI which was possessed at the time of proposing the plan is still not made public on the day of execution, then such execution might be delayed.

## CONCLUSION

It is very clear from this discussion that the laws prohibiting the practice of insider trading have evolved to a great extent from its onset. The laws have just gotten stringent with every new legal statute. This has gone onto show us that the authorities consider this malpractice as an alarming issue and have tried implementing new and stringent statutes to curb it. With this attitude of the authorities, it is implied that they take this issue seriously and any violation of the laws in this particular area will be dealt with great consequences. Hence, it is important for every person engaging in stock trading to be aware of these prohibitions and exceptions as laid down in the legal statute and indulge in legal trading in order to avoid great deal of scrutiny and consequences in the future.

# Unit 12: Company Meetings and Proceedings

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CONTENTS



## Objectives

After studying this unit, you will be able to:

- Describe provisions relating to statutory meetings;
- Explain provisions relating to annual general meetings;
- Explain extraordinary meeting;
- Describe voting and poll.

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## Introduction

A company is an artificial person and therefore, cannot act itself. It must act through some human intermediary. The various provisions of law empower shareholders to do certain things. They are specifically reserved for them to be done in company's general meetings. Section 291 empowers the Board of directors to manage the affairs of the company. In this context meetings of shareholders and of directors become necessary. The Act has made provisions for the following different types of meetings of shareholders: (i) Statutory Meeting; (ii) Annual General Meeting; (iii) Extraordinary General Meeting; and (iv) Class Meetings.

## 12.1 Statutory Meeting (S.165)

Some of the most important legal provisions regarding the statutory meetings are:

1. It is required to be held only by a public company having a share capital. A private company or a public company registered without share capital is under no obligation to hold such a meeting.
2. It must be held within a period of not less than one month and not more than six months from the date at which the company is entitled to commence business.
3. At least 21 days before the day of meeting, a notice of the meeting is to be sent to every member stating it to be a statutory meeting.
4. The Board of directors should also get a report, called the statutory report, sent to each member along with the notice of the meeting. If the statutory report is forwarded later, it shall be deemed to have been duly forwarded if it is so agreed to by all the members entitled to attend and vote at the meeting. A copy of the statutory report should also be sent to the Registrar after the same is sent to the members.

   The statutory report contains (a) the total number of shares allotted – fully paid-up and partly paid-up; allotted for cash and for consideration other than cash; (b) the total cash received by the company in respect of all allotments; (c) an abstract of receipts and payments up to a date within seven days of the date of the report and the balance of cash in hand; (d) any commission or discount paid on the issue of shares or debentures; (e) the names, addresses and occupations of directors, auditors, managers and the secretary of the company; (f) the extent to which any underwriting contract has not been carried out; (g) the arrears due on calls from every director; (h) the particulars of any commission or brokerage paid to any director or manager on the issue of shares and debentures.

   The statutory report is required to be certified as correct by at least two directors, one of whom shall be the managing director, where there is one. Also, the auditors of the company shall certify that part of the statutory report which relates to the shares allotted, cash received thereon and the receipts and payments and the balance of cash in hand.
5. The members present at the meeting may discuss any matter relating to the formation of the company or arising out of the statutory report without previous notice having been given.
6. The meeting may adjourn and the adjourned meeting has the same powers as the original meeting. The adjourned meeting, therefore, may do anything which could have been done by the original meeting.
7. If default is made in complying with the provisions of s.165, the following consequences may follow: (a) Every director or other officer of the company who is in default shall be punishable with fine up to ₹ 5,000. (b) The Registrar or a contributory may apply to the

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court for the winding up of the company [s.439]. However, the court may, instead of passing an order for winding up, give directions for the holding of the meeting for filing of the statutory report.

8. It should be remembered that this meeting is required to be held only once in the life time of a public company, having a share capital.

## 12.2 Annual General Meeting (AGM) (SS.166-168)

As the name signifies, this is an annual meeting of a company. The provisions relating to this meeting are:

1. Every company, whether public or private, having a share capital or not, limited or unlimited must hold this meeting.

2. The meeting must be held in each calendar year and not more than fifteen months shall elapse between two meetings. However, the first AGM may be held within eighteen months from the date of its incorporation and if such general meeting is held within that period, it need not hold any such meeting in the year of its incorporation or in the following year. The maximum gap between two such meetings may be extended by three months by taking permission of the Registrar, who may so allow for any special reason.

   The Company Law Department has expressed the view that the Registrar can grant extension of time, for special reasons, up to a maximum period of 3 months, even if such extension allows the company to hold its AGM beyond the calendar year. However, the said extension shall be granted only if the application therefor is made to the Registrar before the expiry of the period as per s.166 (1).

3. The meeting must be held (i) on a day which is not a public holiday, (ii) during business hours, (iii) at the registered office of the company or at some other place within the city, town or village in which the registered office is situated. [s.166(2)].

4. The business to be transacted at such a meeting may comprise of (s.173):

   (i) Ordinary business which relates to the following matters: (a) consideration of accounts, balance sheet and the reports of the Board of directors and auditors; (b) declaration of dividend; (c) appointment of directors in the place of those retiring; and (d) appointment of auditors and fixation of their remuneration.

   (ii) Any business other than ordinary business transacted at the meeting will be deemed to be special business. With regard to all special business, an Explanatory Statement is required to be annexed to the notice.

5. What about a situation where annual accounts are not ready for being placed before the AGM? In case annual accounts are not ready for laying at the appropriate AGM, it is open to the company concerned to adjourn the said AGM to a subsequent date when the annual accounts are expected to be ready for approval in the AGM. Since consideration of annual accounts is only one of the matters to be dealt with at an AGM, directors are under a statutory obligation to hold the meeting. The proper course shall be to hold the meeting and then adjourn it to a suitable date for considering the accounts. The adjourned meeting must, however, be held within the maximum time limit allowed under s.166.

6. The combined reading of Ss.166 and 210 requires compliance with the following: (a) There must be one meeting held in each calendar year. (b) Not more than 15 months must elapse between one general meeting and another. (c) The period of 15 months may be extended to 18 months by the Registrar. (d) Except in the case of the first AGM, the accounts must relate to a period beginning with the day immediately after the period for which they

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were submitted and ending with a day which must not precede the day of the meeting by more than 6 months; or 6 months and the extension granted by the Registrar, i.e., a maximum period of 9 months.

7. The company must give twenty-one days notice to all the members of the company and the auditor. A shorter notice may be held valid if consent is accorded to, by all the members entitled to vote at the meeting (s.171). Such a consent may be given before the meeting is held or after the resolutions are passed. A copy of Directors' report on the company's position for the year together with copy of the audited accounts and auditors' report must accompany the notice. Also a proxy form must be attached with the notice, on which it shall be specifically mentioned that a member entitled to vote is entitled to appoint proxy, and such proxy need not be a member of the company.

   The notice must specify the place and the day and hour of the meeting and shall contain a statement of the business to be transacted thereat [s.172(1)].

   If the time of holding the meeting and other essential particulars required by the section are not specified in the notice, the meeting will be invalid and all resolutions passed thereat will be of no effect.

   The notice must be given to every member, legal representative of a deceased member or assignee of an insolvent member and to auditor or auditors [s.172(2)].

8. If default is made in holding the meeting, the Central Government may, on the application of any member of the company, call or direct the calling of the meeting. If the company fails to hold the meeting either originally or when directed to do so by the Central Government, then the company and every officer of the company who is in default shall be punishable with fine up to ₹ 50,000; and in the case of a continuing default, with a further fine of ₹ 2500 per day during the continuance of default (s.168).

### 12.2.1 Certain Typical Issues in Respect of AGM

1. ***Whether AGM can be called on a Public Holiday***: Section 166(2), *inter alia*, provided that, every AGM shall be called on a day that is not a public holiday. The Department of Company Affairs has opined that, it is a mandatory provision.

   However, Bank holidays (for purposes of closing) though declared as public holidays under the Negotiable Instruments Act, 1881 shall not be treated as public holidays for the aforesaid purpose. Thus, 31st March and 30th Sept. shall not be considered as public holidays.

   In the following cases, however, AGM may be held on a public holiday: (i) Section 2(38) provides that, if any day is declared by the Central Government to be a public holiday after the issue of the notice convening such a meeting, it shall not be deemed to be a public holiday in relation to the meeting. (ii) Where a public company or its subsidiary has by its Articles fixed the time of its AGM and the day turns out to be a public holiday [Proviso (a) to s.166(2)]. (iii) Where a public company or its subsidiary has, by a resolution passed in one AGM fixed the time for its subsequent AGM and the day turns out to be a public holiday [Proviso (a) to s.166(2)]. (iv) A private company which is not a subsidiary of a public company may also [like a public company or its subsidiary under (ii) and (iii) above] by a resolution agreed to all the members thereof fix the time as well as the place of its AGM and the same shall be valid if the day happens to be a public holiday [Proviso (b) to s.166(2)]. (v) A company to whom a license is granted under s. 25 is exempted from the provisions of s.166(2). (vi) Where the AGM is adjourned because of lack of quorum, it is to be held on the same day in the next week at the same time and place (s.174). In case the day comes to be accidentally a public holiday, it shall not amount to contravention of s.166(2).

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2. ***Whether it is not obligatory to advertise notice of meetings in the newspapers:*** However, as an abundant precaution, the company may advertise in the newspapers to avoid objection from such of the shareholders as reside outside India and who incidentally may not receive the notices served through post.

3. ***Voting Rights of Members:*** It shall be determined as at the date of the meeting and not as they would have been if the meeting had been held within the prescribed time.

4. M***eeting Beyond Statutory Time:*** It cannot be said to be void or illegal. If the central government does not extend the date of holding the AGM u/s 167, the directors shall be subjected to increasing penalty but the meeting shall be a valid meeting. Otherwise, the position in law would become impossible.

5. ***Power to Cancel or Postpone:*** The Board of directors has the power to cancel or postpone a meeting convened, though it cannot be exercised except *for bona fide* and proper reasons.

*Task* A company served a notice of a general meeting to its members. The notice stated that a resolution to increase the share capital of the company would be considered at such meeting. A shareholder complains that the amount of the proposed increase was not specified in the notice. Is the notice valid?

### Self Assessment

Fill in the blanks:

1. ..... is required to be held only by a public company having a share capital.
2. In statutory meeting the Board of directors should also get a report, called the .....
3. The statutory report is required to be certified as correct by at least two directors, one of whom shall be the managing director, and other .....
4. ..... meeting must be held in each calendar year and not more than fifteen months shall elapse between two meetings.

## 12.3 Extraordinary Meeting (EGM) (S.169)

Every general meeting (i.e. meeting of members of the company) other than the statutory meeting and the annual general meeting or any adjournment thereof, is an extraordinary general meeting. Such meeting is usually called by the Board of Directors for some urgent business which cannot wait to be decided till the next AGM. Every business transacted at such a meeting is special business. An explanatory statement of the special business must also accompany the notice calling the meeting. The notice should also give the nature and extent of the interest of the directors or manager in the special business, as also the extent of the shareholding interest in the company of every such person. In case approval of any document has to be done by the members at the meeting, the notice must also state that the document would be available for inspection at the Registered Office of the company during the specified dates and timings.

The Articles of Association of a Company may contain provisions for convening an extraordinary general meeting. E.g., it may provide that "the board may, whenever it thinks fit, call an extraordinary general meeting" or it may provide that "if at any time there are not within India, directors capable of acting who are sufficient in number to form a quorum, any director or any two members of the company may call an extraordinary general meeting".

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### 12.3.1 Extraordinary General Meeting on Requisition

The members of a company have the right to require the calling of an extraordinary general meeting by the directors. The board of directors of a company must call an extraordinary general meeting if required to do so by the following number of members:

- Members of the company holding at the date of making the demand for an EGM not less than one-tenth of such of the voting rights in regard to the matter to be discussed at the meeting.
- If the company has no share capital, the members representing not less than one-tenth of the total voting rights at that date in regard to the said matter.

The requisition must state the objects of the meetings and must be signed by the requisitioning members. The requisition must be deposited at the company's registered office. When the requisition is deposited at the registered office of the company, the directors should within 21 days, move to call a meeting and the meeting should be actually be held within 45 days from the date of the lodgement of the requisition. If the directors fail to call and hold the meeting as aforesaid, the requisitionists or any of them meeting the requirements at (a) or (b) above, as the case may be, may themselves proceed to call meeting within 3 months from the date of the requisition, and claim the necessary expenses from the company. The company can make good this sum from the directors in default. At such an EGM, any business which is not covered by the agenda mentioned in the notice of the meeting cannot be voted upon.

Clause 47 of Table A (Schedule I) provides that, all general meetings other than AGMs shall be called the EGMs. The legal provisions as regards such meetings are:

1. EGM is convened for transacting some special or urgent business that may arise in between two AGMs, for instance, change in the objects or shift of registered office or alteration of capital. All business transacted at such meetings is called special business. Therefore, every item on the agenda must be accompanied by an 'Explanatory Statement'.
2. An EGM may be called: (i) by the directors on their own accord; (ii) by the directors on requisition; (iii) by the requisitionists themselves; (iv) by the Company Law Board. The board of directors may call a general meeting of the members at any time by giving not less than 21 days notice. A shorter notice may, however, be held valid if consent is accorded thereto by members of the company holding 95% or more of the voting rights (s.171). The board of directors must convene a general meeting upon request or requisition if the following conditions are satisfied (s.169):

   The requisitionists must be such number of members who, at the date of the deposit of the requisition, are the holders of 1/10th of total voting power. Thus, in case of a company having a share-capital they should hold at least 1/10th of such of the paid-up capital that carries right to vote in regard to that matter. Preference shareholders have voting power only as regards matters relating to the preference shareholders. They have no voting right and therefore, no right to requisition in respect of other matters. If the company does not have a share capital, they should at least hold 1/10th of the total voting power of the company in regard to that matter. The requisition must state the objects of the meeting, i.e., it must set out the matters for the consideration of which the meeting is to be called. Further, requisition must have been deposited at the registered office of the company. The requisition must be signed by the requisitionists. In case all the aforesaid conditions are satisfied, the board of directors must within 21 days of the receipt of the requisition call the meeting giving at least 21 days notice fixing the meeting within 45 days of the receipt of the requisition.

Where the resolution proposed is a special resolution then the requirements of s.189(2) must be complied with, viz., it should be so described and explanatory statement be annexed.

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If the board of directors does not/fails to call the meeting as aforesaid (i.e., at least 21 days notice fixing the date of the meeting within 45 days of the deposit of a valid requisition), the meeting may be called by the requisitionists themselves: (a) In case of a company having share capital, by one or more requisitionists as represent: (i) a majority in value of the paid-up share capital held by all the requisitionists; or (ii) at least 1/10th of the paid-up share capital carrying voting rights in respect of that matter, whichever is less; or (b) in case of a company not having a share capital, by one or more requisitionists who represent at least 1/10th of the total voting power of the company in regard to the matter of the requisition.

Where the Articles, in accordance with the provisions of s.180, provide that members who have not paid calls on their shares would not be entitled to vote, then they cannot requisition a meeting, nor vote at it and if they do so, the proceedings would be invalid.

The requisitioned meeting must be held within 3 months of the date of the deposit of the requisition. Further, where two or more persons hold any shares or interest in a company jointly, a requisition, or a notice calling a meeting, signed by one or only some of them shall, for the purposes of this section, have the same force and effect as if it had been signed by all of them.

Any reasonable expenses incurred by the requisitionists, as aforesaid, shall be repaid to them by the company and the same shall be recouped from directors at fault.

A meeting by the requisitionists must be held in the same manner as nearly as possible, in which the meetings are to be called by the board of directors. However, where the registered office is not made available to them for holding the meeting, they may hold the meeting elsewhere [R. Chettair vs. M. Chettair (1951) 21 Comp. Cas. 93].

### Powers of the Company Law Board (s.186).

If for any reason it is impracticable to call a meeting of the company, other than an AGM, the Company Law Board may direct the calling of the meeting: (a) on its own motion; (b) on an application of any director; (c) on an application of any member entitled to vote at that meeting.

For the aforesaid meeting, the Company Law Board may give directions in respect of the place, date and the manner in which the meeting be held and conducted. It may also give such ancillary or consequential directions as it thinks expedient, including a direction that one member present in person or proxy shall be deemed to constitute a meeting.

*Example:* Superclean Industries Pvt. Ltd. is a company in which there are three shareholders and all of them are directors of the company. Mr. Superman holds 60 percent of the paid up share capital while the balance 40 percent of shares is held equally by the remaining two directors. Because of some rift among them, the two directors holding 40 percent share capital have aligned and started preventing the holding of any meetings of the company. The articles of the company provide for a minimum of two directors/members as quorum for board meetings as well as general meetings.

Mr. Superman is a majority shareholder, but he is helpless, as no meeting can be held because of no quorum. He would apply to CLB under s. 186 for convening of the general meeting. The CLB, if satisfied, will order a meeting to be held with the presence of one member as sufficient quorum. Mr. Superman, being the majority shareholder is entitled to exercise his statutory right to participate in the decision-making process, which cannot be frustrated by the quorum requirement. [Opera Photography Ltd. Re, 1989 B CLC 763 CLD]

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### Self Assessment

5. Which of the following are included in the 'Statutory Books' for the purpose of company audit?

   (i) Register of charges

   (ii) Minutes Books for the Board meetings

   (iii) Articles of Association

   (iv) Minutes Book for the shareholder's meeting

   (v) Register of members

   (vi) Memorandum of Association

   Select the correct answer using the codes given below:

   Codes

   (a) (i), (ii), (iv) and (v) (b) (ii), (iii), (iv) and (vi)

   (c) (i), (iii), (v) and (vi) (d) (ii), (iii), (v) and (vi)

6. Consider the following statements: A statutory auditor of a public limited company claims that he has the following legal rights in relation to his duties:

   (i) Right to refuse to make a report

   (ii) Right of access to books of accounts and registers

   (iii) Right to seek explanation from directors and officers

   (iv) Right to make statement in the general meeting.

   Of the above statements:

   (a) (i), (ii) and (iii) are correct (b) (i), (ii) and (iv) are correct

   (c) (i), (iii) and (iv) are correct (d) (ii), (iii) and (iv) are correct

## 12.4 General Meeting for Shareholders

When it is proposed to alter, vary or affect the rights of a particular class of shareholders (e.g., where accumulated dividends on cumulative preference shares are to be cancelled) and it is not possible to obtain the consent in writing, of the holders of 3/4th of the issued shares of that class, a meeting of the holders of those shares may be called. Such a meeting is commonly known as a 'class meeting'. It should be noted that all resolutions in a class meeting must be passed as special resolutions.

The holders of at least 10% of the issued shares of that class who did not consent in favour of the resolution may apply to the court within 21 days to have the resolution cancelled and where such application is made, the resolution shall not have effect unless and until it is confirmed by the court.

*Task* A meeting was properly convened and was subsequently adjourned by the chairman. No fresh notice is given for the adjourned meeting which is held subsequently. State whether the adjourned meeting is valid. [***Hint:*** The adjourned meeting in question is valid as per s.174.]

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## 12.5 Requisites of a Valid Meeting

### 12.5.1 Notice of Meeting

Every member of the company is entitled to a notice of every general meeting. A notice of not less than 21 days must be given in writing to every member. However, a shorter notice for AGM will be valid if all members entitled to vote give their consent. In case of other meetings, a shorter notice will be valid if consent is given by members holding at least 95% of the paid-up capital carrying voting rights, or representing at least 95% of the voting power.

The notice may be given to members either personally, or sending by post to him at his registered address. A notice of a meeting may also be given by advertising the same in a newspaper circulating in the neighbourhood of the registered office of the company.

The secretary should see that proper notice of meeting must be given to all persons who are entitled to receive it. An improper or insufficient notice, as well as absence of notice, may affect the validity of a meeting and render the resolutions passed at the meeting ineffective. Also the notice should make a full and frank disclosure to the members of the fact on which they would be expected to vote.

### 12.5.2 Agenda of the Meeting

The word 'agenda' indicates the business to be transacted at a meeting. It is prepared for all kinds of meetings in order that the meeting may be conducted systematically. The agenda is generally prepared by the secretary in consultation with the chairman. It is drafted in such a manner as to help the chairman to conduct the meeting smoothly. In drafting the agenda, the secretary should bear in mind the following: (i) the agenda should be clear and explicit; (ii) it should be drafted in a summary manner; (iii) all items of routine business should be put down first and the contentious matters later; and (iv) all items of similar nature should be placed in a continuous order.

The foregoing points are important because when a copy of the agenda is sent to a member, he is in a position to form a definite opinion of the subject matter to be discussed at the meeting. While preparing the agenda, care should be taken for the order of the matters to be discussed, as the order of the agenda cannot be altered except with consent of the meeting. Sometimes, the agenda is drafted in such a manner that it can serve the purpose of minutes later on. Some space is left opposite each agenda item and the secretary writes it up during the meeting; this practice is very common in the preparation of agenda for Board meetings.

Sometimes, companies maintain an Agenda Book, wherein the agenda items are entered. It is placed before the chairman of the meeting and is regarded as the agenda. Those placed before the members or other directors are copies only. Later, the agenda book becomes a permanent record for future reference.

### 12.5.3 Proxy

In the case of a company, every member of the company entitled to attend and vote at a meeting has the right to appoint another person, whether a member or not, to attend and vote for him. The term 'proxy' is applied to the person so appointed. Also, it refers to the instrument by which a member of a company appoints another person to attend the meeting and vote on his behalf. However, the proper term for this document is 'proxy form' or 'proxy paper'. The following points about proxies are to be noted: (i) A proxy has no right to speak at the meeting. (ii) A proxy

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need not be a member of the company. (iii) The instrument appointing a proxy must be in writing and signed by the appointor. (iv) The proxy form must bear the date of the meeting. (v) No company can make it compulsory for anyone to lodge proxies earlier than 48 hours before the meeting. (vi) A proxy may be revoked before the person appointed has voted. (vii) A proxy can demand a poll. (viii) A proxy cannot vote against the wishes of his appointor.

### Secretarial work as regards proxies

(a) Scrutinise the proxy forms to see whether they comply with the provisions of the Act, and the bye-laws and rules of the company. (b) Any proxies received after the stipulated time limit must be returned with a note that they cannot be accepted. (c) Any irregularities in proxy forms should be reported to chairman of the meeting, as he is the final authority to accept or reject them. (d) Each correct proxy form is countersigned by the secretary. (e) Enter the correct proxy forms in the register of proxies. (f) Return the proxy form to the member together with an admission card in the name of the proxy.

## 12.5.4 Voting and Poll

Unanimity on all matters before a meeting is always not obtained. In the absence of unanimity, the chairman wants to know the wishes of the persons present therein. This is known as ascertaining the sense of the house and for this purpose; he has to put the matter before the house to the members. There are various methods which can be adopted by the chairman to put the matter to vote in order to ascertain the wishes of the members.

In the case of a company, the Act prescribes two methods to ascertain the wishes of the members. These are:

(i) ***By Show of Hands:*** Under this method, the chairman asks all those in favour of the resolution to raise their right hand and when that number is noted, asks all those against to do likewise. The chairman then declares the result of the voting indicating whether the proposal has been carried or lost.

(ii) ***By Poll:*** In company meetings, voting by poll is according to the number of shares held by a member. Under this method, every person present records his vote on a ballot paper and deposits it in the ballot box provided for that purpose. The counting of ballots cast for and against the motion reveals the results. This method ensures secrecy in casting votes. The voting by show of hands may not always reflect the opinion of members upon a value basis. Also, there may be a number of proxies who can vote only by poll and not by show of hands.

### Rules in respect of voting

As per the provisions of the Act, rules regarding voting may be noted as follows:

1. Every holder of equity shares shall have a right to vote [s. 87(1)].
2. Right of an equity shareholder to vote cannot be prohibited on the ground that, he has not held his shares for any specified period before the meeting or on any other ground (s.182). In Ananthalakshmi vs. H. I. & F. Trust, AIR 1951 Mad. 927, a provision in the Articles of a company that only those shareholders would be entitled to vote whose names have been there on the register for two months before the date of the meeting was held to be in contravention of the Act.

   The only ground on which the right to vote may be excluded is non-payment of calls by a member or other sums due against a member or where the company has exercised the right of lien on his shares (s.181).

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3. A preference shareholder shall have the right to vote only on resolutions which directly affect the rights attached to his preference shares [s.87(2)].

   Where the directors proposed to increase the shares of the company (i) by issue of further equity shares, or (ii) by capitalising an amount standing to the credit of the company's reserve account and applying the same in paying-up the new equity shares and distributing the same as fully paid among the equity shareholders, the proposed resolution was held to affect the rights of the preference shareholders and could, therefore, be only carried out with their sanction [Re John Smith's Tadcaster Brewery Co. Ltd. (1952) 2 All ER 751].

4. Voting rights of a member are not affected by the fact that his shares have been attached or pledged or a receiver has been appointed [Balkrishnan Gupta vs. Swadeshi Polytex Ltd. (1985) 58 Comp Cas. 563].

5. Voting by show of hands in the first instance. Section 177 provides that, at any general meeting, a resolution put to vote shall, unless a poll is demanded under s.179, be decided on a show of hands. A declaration by the chairman that on a show of hands, a resolution has or has not been carried either unanimously or by a particular majority and an entry to that effect in the minutes book of the company, shall be conclusive evidence of the fact. No proof of the number or proportion of the votes cast in favour of or against such resolution shall be required (s.178).

### Demand for Poll

Section 179 provides that before or on declaration of the result of the voting on any resolution on a show of hands, a poll may be ordered to be taken by the Chairman of the meeting of his own motion and shall be ordered to be taken by him on a demand made in that behalf by the person or persons specified below:

(a) In the case of a public company having a share capital, by any member or members present in person or by proxy and holding shares in the company: (i) which confer a power to vote on the resolution not being less than 1/10th of the total voting power in respect of the resolution; or (ii) on which an aggregate sum of not less than fifty thousand rupees has been paid-up;

(b) In the case of a private company having a share capital, by one member, present in person or by proxy if not more than seven members are personally present and by two members present in person or by proxy, if more than seven members are personally present;

(c) In the case of any other company, by any member or members present in person or by proxy and having not less than 1/10th of the total voting power in respect of the resolution.

The chairman of the meeting may regulate the manner in which the poll should be taken. He must appoint two scrutinisers to scrutinise the votes given on the poll and to report thereon to him. Then the chairman will declare the result.

Voting by companies, and Government as members (Ss.187-187-A). Where a company or a corporation is a member of another company, it may attend the meetings of the other company through a representative. The representative must be appointed by a resolution of the Board of directors or the other governing body. Where the Central Government or a State Government is a member, the President or the Governor of the State, as the case may be, has the power to appoint representatives to attend meetings of the company. The person nominated shall hold the position of a proxy.

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### Self Assessment

7. Can a Company hold an AGM on public holiday?
   (a) Yes (b) No
   (c) (a) and (b) both are correct (d) None
8. Audit of a public company will be counted for the limit of audits
   (a) Yes (b) No
9. Statutory meeting must be held in case of a public company
   (a) Yes (b) No
10. Statutory meeting must be held in case of a private company
   (a) Yes (b) No

## 12.6 Resolutions

Decisions of a company are taken by resolution of its members, passed at their meetings. Also, the Board of directors takes certain decisions at its meeting by passing certain resolutions after due deliberations.

The term 'motion' indicates a proposition made at a meeting by any member. Such a motion may be passed without any change or modification. But if some members feel that the motion in the form proposed needs some change or modification, they may move an amendment. A motion when passed with or without amendment is called a resolution.

A motion should always be in writing and before it is brought before the meeting, the necessary notice must be given. A person proposing a motion is called the mover and the motion should be signed by him.

Once the motion has been put to the members and they have voted in favour of it, it becomes a resolution. In the case of a company, there are three kinds of resolutions:

1. Ordinary resolution;
2. Special resolution;
3. Resolution requiring special notice.

*Task* One general meeting was called by a company in December, 2004. This meeting was adjourned to March, 2005 and then held. Subsequent meeting was held in February; 2006. Is the company liable for any irregularity?

### 12.6.1 Ordinary Resolution [s.189(1)]

When a motion is passed by a simple majority of the members voting at a general meeting, it is said to have been passed by an ordinary resolution. In other words, votes in favour of the resolution are more than 50%. Still in other words, a resolution shall be an ordinary resolution where the votes cast in favour of the resolution are more than the votes cast against the resolution. According to s.189(1), "A resolution shall be an ordinary resolution when at a general meeting of which the notice required under the Act has been duly given, the votes cast (whether on show

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of hands, or on poll, as the case may be), in favour of the resolution (including the casting vote, if any, of the chairman) by members who, being entitled to do so, vote in person or where proxies are allowed, by proxy, exceed the votes, if any, cast against the resolution by members so entitled and voting."

All matters which are not required either by the Act or the company's Articles to be done by a special resolution can be done by means of an ordinary resolution. Some of the cases in which only ordinary resolution is required are: alteration of authorised capital, declaration of dividend, appointment of auditors, election of directors.

### 12.6.2 Special Resolution [s.189 (2)]

A resolution is a special resolution in regard to which: (a) the intention to propose the resolution as a special resolution has been specifically mentioned in the notice calling the general meeting; (b) 21 days notice has been duly given for calling the meeting; (c) the number of votes cast in favour of the resolution is three times the number cast against it.

Some of the cases in which a special resolution is necessary: alteration of objects clause; change of registered office from one State to another; alteration of the Articles; changes in the name of the company; reduction of share capital.

### 12.6.3 Resolution Requiring Special Notice (s.190)

Some resolutions require special notice. The object of special notice is to give the members sufficient time to consider the proposed resolution and also to give the Board of directors an opportunity to indicate views, on the resolution if it is not proposed by them but by some other shareholders. Under this, a notice of intention to move the resolution should be given to the company not less than 14 days before the date of the meeting at which it is proposed to be moved. The company in turn must immediately give notice by advertisement in a newspaper or in any other mode allowed by the Articles, but not less than seven days before the meeting. Some of the cases in which a special notice is necessary are: appointing an auditor, a person other than a retiring auditor; moving a resolution that a retiring auditor will not be re-appointed; removing a director before his term expires.

Section 192 requires that a printed or a type written copy of each special resolution should be sent to the registrar within 30 days of passing thereof.

### 12.6.4 Passing of Resolutions by Postal Ballot (s.192A)

Section 192A contains the following provisions for passing of resolution by postal ballot:

(i) A listed company may and in the case of resolution relating to such business as the Central Government may, by notification, declare to be conducted only by postal ballot, shall, get any resolution passed by means of a postal ballot, instead of transacting the business in general meeting of the company.

(ii) Where a company decides to pass any resolution by resorting to postal ballot, it shall send a notice to all the shareholders, along with a draft resolution explaining the reasons therefor, and requesting them to send their assent or dissent in writing on a postal ballot within a period of 30 days from the date of posting of the letter.

(iii) The notice shall be sent by registered post acknowledgement due, or by any other method as may be prescribed by the Central Government in this behalf and shall include with the notice, a postage pre-paid envelope for facilitating the communication of the assent or dissent of the shareholder to the resolution within the said period.

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(iv) If a resolution is assented to by a requisite majority of the shareholders by means of postal ballot, it shall be deemed to have been duly passed at a general meeting convened in that behalf.

(v) If a shareholder sends under (ii) above his assent or dissent in writing on a postal ballot and thereafter any person fraudulently defaces or destroys the ballot paper or declaration of identity of the shareholder, such person shall be punishable with imprisonment for a term which may extend to 6 months or with fine or with both.

(vi) If a default is made in complying with provisions in (i) to (iv), the company and every officer of the company, who is in default shall be punishable with fine which may extend to ₹ 50,000 in respect of each such default.

### 12.6.5 Circulation of Members' Resolution (s.188)

When some members of a company want (i) to propose a resolution at the company's next AGM; or (ii) desire to circulate to members any statement with respect to the matter referred to in any proposed resolution or any business to be dealt with at any general meeting, the Act allows them to use the administrative machinery of the company for the purpose.

If the requisite number of members make a requisition as aforesaid, the company shall be bound to: (i) give a notice of the resolution intended to be moved at the next AGM; (ii) circulate the statement among the members entitled to notice of any general meeting. However, before the obligation of the company in respect of the above may arise, the following conditions shall have to be satisfied:

- The requisition must have been signed by at least: (a) members having 1/20th of the total voting rights of all the members having the right to vote on the resolution; or (b) members, numbering 100 (having the right to vote at the resolution) and commanding a paid-up share capital of ₹ 1 lakh or more.
- The requisition must have been deposited at the registered office of the company: (a) at least 6 weeks before the meeting in case of a requisition requiring notice of a resolution; and (b) at least 2 weeks before the meeting in case of any other requisition.
- The statement to be circulated should not contain more than 1000 words.
- The requisitionists must have deposited with the company a sum reasonably sufficient to meet the expense of the requisition.

### Self Assessment

State whether the following statements are true or false:

11. Every Public Limited Company having a share capital must hold a statutory meeting.
12. A company required to hold a statutory meeting must hold the meeting within one month of obtaining the certificate to commence business.
13. The first AGM of a company must be held within 18 months of the date of incorporation.
14. If a company fails to call or hold an AGM within the prescribed time, the central government may direct the calling and holding of the meeting on a petition of any member.
15. The statutory report is required to be certified as correct by at least two directors, one of whom shall be the managing director, if any.

# BOARD MEETING THROUGH VIDEO CONFERENCING

Company is an Artificial Person created by Law. Company is run by Board of Directors. Board of Directors is appointed by Shareholders of the company. Major decisions for the benefit of company are taken by Board of Directors on behalf of shareholders in the best interest of the company and for enhancing shareholders value. The decisions of Board of Directors of company after their approval are translated into resolutions of the company. Resolutions pave way for smooth conduct of business of the company.

To take decisions and passing of resolutions by Board of Directors, the Directors need to meet personally at the registered office or other place as agreed by Directors. The Board of Directors need to meet every three months and minimum four board meetings should be held in every year.

Video conferencing mode of holding board meeting online is a modern technological gift to companies for conducting board meetings virtually. Virual Board meetings save valuable time, money of Directors. The Directors can focus more on agenda items of board meetings properly and take sound decisions. In present COVID-19 and Pandemic Situation, Video conferencing/Virtual Board Meetings is a boon to corporate and Directors.

Some of the provisions of the Companies Act, 2013 with respect to holding Board Meeting through Video Conferencing are discussed as follows:

- As per Section 173(2) of **Companies Act, 2013** (the Act) read with Rule 3 of the **Companies (Meetings of Board and its Powers) Rules, 2014** (the Rules), every Company **can** hold a **Board Meeting through video conferencing** or other audio-visual means, which are capable of recording and recognizing the participation of the Directors. Storage of data and safe keeping of recorded meeting is important and Company Secretary can play vital role. Various Video conferencing meeting platform include Zoom Meetings, Blue jeans Meetings, Skype Meetings, Google Meet. Link for Board meeting through video conferencing mode should be generated and shared with eligible directors well on time.
- The **quorum** for a **meeting** of the **Board of Directors** of a company shall be [1][one third of its total strength or two directors, whichever is higher], and the participation of the directors by video conferencing or by other audio visual means shall also be counted for the purposes of **quorum** under this sub-section.
- Under section 173 and Para 2.1 of Secretarial Standard-1, companies, whether public or private limited companies must, hold a minimum of four board meetings between the directors in a calendar year. It is essential to note that the gap between two consecutive meetings of the board should not be more than one hundred and twenty days.(Now gap between two Board Meetings should not exceed 180 days).
- Under section 173(3) and Para 1.3 of Secretarial Standard-1, an advance notice of Board Meeting duly signed by any one Director of seven days must be sent to all directors prior to the meeting in writin**g**. Such notice about the meeting must be sent through the post, by hand, or by e-mail or any other electronic medium. The notice must contain relevant details informing the directors about the option available to the directors to attend the **board meeting through video conferencing** or any other audio-visual means and all additional relevant information to allow the directors to attend the meeting through video conferencing or any other audio-visual means .Agenda for the Board meeting may be enclosed with the Notice convening Board Meeting.
- Before commencement of Board Meeting through Video Conferencing mode, a roll call will be taken at the start of the meeting by the chairperson, and every director participating in the board meeting through video conferencing or any other audio-visual means must state, for the record, namely:

1) Full Name of Director and his DIN Number

2) Location from where he is speaking

3) Declaration from Director orally that he received Notice and Agenda of Board Meeting

4) Oral declaration that in Video Conferencing mode and room of board Meeting, no other person is present.

**5)** Attendance of Directors is ascertained during this roll call and shall be considered as a Quorum **for Board Meeting.**

**6)** All safety measures including confidentiality of meeting and protection of call data at the board meeting be the top priority of management of company including Company Secretary**.**

- **Conduct of Board Meeting**: Under sub-rules 8, 9, and 11 of Rule 3 of Companies Rules (Meetings of board and its power), 2014, once the quorum is fulfilled, the chairman shall further proceed for transacting businesses specified in the agenda of the meeting. The participants are required to identify themselves for the record before discussing any item of business in the agenda.

In case passing a Resolution is objected, and there is a need to put it to vote, the chairperson will record the votes of every director who is participating, including the director who attends the meeting through video conferencing. Finally, the Resolution shall be passed on the decision of the majority once the chairperson makes a note of each vote by the director.

Whenever a discussion is completed on an agenda item, the chairperson will declare the summary of the decision made on such an item. The name of the directors shall also be announced who dissented from the decision of the majority. Based upon decisions made and resolutions passed, the company secretary shall prepare minutes of Board meeting held through video conferencing.

- Based upon Video & Audio recordings of Board meeting, the Company Secretary should prepare minutes of Board meeting and sent to Chairman of meeting of his signature. Signed minutes to be circulated to all present directors.
- Matters which can be discussed at a Board meeting convened through Online Video Conferencing mode are as follows : All items of business including following business :

  (a) Approval of the annual financial statement;

  (b) Approval of the Board's report;

  (c) Approval of the prospectus;

  (d) Audit Committee meetings for consideration of financial statement including consolidated financial statement if any, to be approved by the board under Section 134(1) of the Act; and

  (e) Approval of the matter relating to amalgamation, merger, demerger, acquisition and takeover.

However, in light of the Covid-19 pandemic, the Ministry of Corporate Affairs, by way of the **Companies (Meetings of Board and its Powers) Amendment Rules, 2020** dated March 19, 2020, inserted the sub-rule (2) to Rule 4 stating that the matters listed above could also be held via video conferencing and other audio visual means until June 30, 2020, which was later extended to September 30, 20200. On December 30, 2020, another amendment notification was issued by the Government of India through the Ministry of Corporate Affairs which extended this date to June 30, 2021. It seems that in view of Current Pandemic situation, Board meetings through Video Conferencing mode shall be a normal mode of holding Board meetings/Annual General meetings.

# E-VOTING MECHANISM UNDER THE COMPANIES ACT, 2013

**1. Section 108**

As per this section CG may prescribed the class or classes of Companies and mechanism in which members may exercise his voting by electronics means.

**2. Rule 20 of Companies (Management and Administration) Rules, 2014**

**Applicable on which type of meeting Rule 20(1)**

On General meeting for which notices are issue on or after the commencement of this rule.

**Applicable on which company Rule 20(2)**

1. Every Listed Company;

2. Every Company having not less than 1000 Members;

**Proviso to Rule 20(2)**

1. Nidhi Company; or

2. Enterprise or institutional investor referred to in chapter XB or chapter XC of the SEBI (ICDR) Regulations 2009 is not required to provide the facility to vote by electronic means.

**Voting by members Rule 20(3)**

Members exercise his right to vote through electronic means and thereafter company shall resolution in accordance with the normal provisions of the Act.

**Prior requirements of E-Voting Rule 20(4)**

1. A notice of the meeting shall be sent to all the members, directors, auditors of the Company either-

    a. by registered post;

    b. through email;

    c. by courier

2. Notice shall also be placed on the website of the company;

3. Contents of the meeting;

a. Notice shall states that the company is providing facility of e-voting system and business may be transacted through such voting;

b. facility for voting, through electronic voting system or ballot or polling paper shall also be made available at the meeting and members attending the meeting who have not already cast their vote by e-voting shall be able to exercise their right at the meeting;

c. the members can cast in remote e-voting and can attend the meeting but cannot vote at the meeting.

4. Notice shall-

a. states the process and manner for voting may by electronic means;

b. Time period during which the votes may be cast by remote e-voting;

c. Login ID details;

d. Generating or receiving the password and for casting of vote in a secure manner;

5. at least 21 days before the days before the date of general meeting-

a. at least once in a vernacular newspaper in the vernacular language of the district in which the registered office of the company is situated and having a wide circulation in that district; and

b. at least once in English language in an English newspaper having country-wide circulation and specifying in the said advertisement inter alia.

The following manners namely:-

1. Statement that business may be transacted through E-Voting;

2. The time schedule of the e-voting;

3. End time of the meeting;

4. cut-off

5. the manner for obtaining e-mail ID and Password;

f. A statement that-

1. Beyond the specified time the remote e-voting shall not be allowed;

2. Manner for providing e-voting facility to the member presents at the meeting;

3. even if the member exercise his vote through e-voting then member may also participate in the meeting but he cannot vote at the meeting;

4. members whose name mentioned in the Register of Members may avail the facility through remote e-voting or E-voting at the meeting.

5. website address of the Company;

6. Particulars of person responsible to address the grievances connected with facility for voting by emails.

**Time of e-voting facility**

6. remote e-voting shall remain open for not less than thee days and shall close at 5.00 p.m. on the date Preceding the date of the general meeting;

**Eligible members**

7. the members of the company, holding shares either in physical form or in dematerialised form, as on the cut-off date, may opt for remote e-voting;

Vote shall not be changed once the vote casted on any resolution;

**End of e-voting**

8. At the end of the remote e-voting period, the facility shall be blocked.

Provided that if the e-voting facility provided by company at the General meeting, the said facility shall remain in operation till the resolutions are considered and voted upon in the meeting.

Only those members who entitled to vote at the meeting and have not voted during remote e-voting.

**Appointment of scrutinizer**

The BOD shall appoint one or more scrutinizer,

The scrutinizer may be CA in Practice, CWA in practice, CS in practice or an Advocate, or any other person who is not in employment of the company and is a person of repute who, in the opinion of the Board can scrutinse the voting and remote e-voting in a fair and transparent manner.

**Function of Scrutinizer**

After conclusion of the meeting, the scrutinizer shall-

a. First count the votes cast at the meeting;

b. unblock the votes cast through remote e-voting in presence of at least 2 witnesses not in the employment of the Company, not later than three days of conclusion of the meeting, a consolidated scrutinizer's report of the total votes cast ln favor or against, if any, to the Chairman or a person authorizedby him in writing who shall countersign the same:

**Declaration of result**

The result shall be declare by the chairman or person authorized.

**Register to be maintained by the scrutinizer**

He shall maintain either electronically or manually a register to record-

a. the assent or dissent received,

b. mentioning the particulars of name, address, folio number or client ID of the members,

c. number of shares held by them, nominal value of such shares

d. and whether the shares have differential voting rights;

**All the documents and register shall be in the custody of the scrutinizer**

It shall remain in the safe custody of the scruitniser until the Chairman considers, approves and signs the minutes and there after, the scrutiniser shall hand over the register and other related papers to the company.

**Result of the voting shall be on the website of the company**

Result along with the report of the scrutinizer shall be placed on the website of the company.

In case company is listed the same shall be forward the result to the concerned stock exchange or exchanges and stock exchange shall place the same on its website.

**Resolution when passed?**

The resolution shall be deemed to be passed on the date of the relevant general meeting if requisite has been received.