

PAYMENT OF MANAGERIAL REMUNERATION DURING COVID- 19





What is Managerial Remuneration?

Remuneration paid or payable to:

Executive Directors

Non-Executive Directors

Manager





Components of Remuneration



As per section 2(78) of the Act, remuneration means the following:

- ✍ any money or its equivalent given or passed to any person for services rendered by him;
- ✍ includes perquisites as defined under the Income Tax Act, 1961.





Components of Remuneration



Salary



Perquisites



Commission on profits

INCLUDES

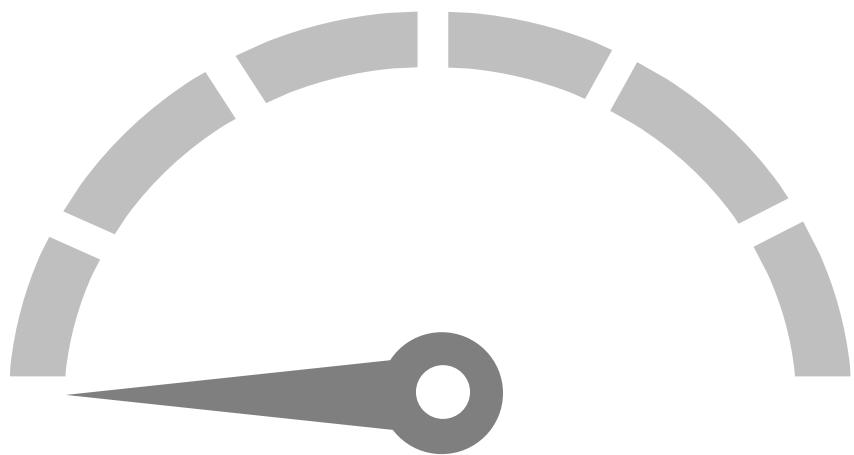
EXCLUDES

**Reimbursement of
expenses**





Maximum Managerial Remuneration



11%

of the net profits of the company
OVERALL LIMIT



5% of the net profits

**Remuneration to any one MD/
WTD/ Manager.**



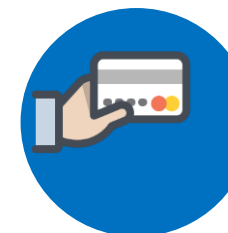
10% of the net profits

**If there is more than one MD/
WTD/ Manager, all such directors
and manager taken together.**



**1% of the net profits, if Company
has executive directors**

Directors who are neither MD nor WTD



**3% of the net profits, if Company
has no executive directors**

Directors who are neither MD nor WTD





Net Profits



- ✍ Net profits shall be calculated in accordance with Section 198 of the Act;
- ✍ Section 198 provides expense & income which are eligible for deduction and addition, respectively
- ✍ Easy way to calculate is to take profit before tax from P & L account and add disallowed expenditure and reduce disallowed income
- ✍ Remuneration paid to Directors shall be added back while calculating net profits.





Modes of Remuneration



Monthly Payment



- ~~✗~~ Executive Directors
- ~~✗~~ Non-Executive Directors except Independent Directors



Sitting Fees



- ~~✗~~ Executive Directors
- ~~✗~~ Non-Executive Directors
- ~~✗~~ Independent Directors



Profit related commission



- ~~✗~~ Executive Directors
- ~~✗~~ Non-Executive Directors
- ~~✗~~ Independent Directors





Sitting Fees



- ✗ A company may pay a sitting fee to a director (including EDs) for attending meetings of the Board or committee thereof.
- ✗ Sitting fees will be as decided Board but shall not exceed INR 1,00,000 per meeting of the Board or committee (statutory and non statutory) thereof.
- ✗ For Independent Directors and Women Directors, the sitting fees shall not be less than the sitting fees payable to other directors.
- ✗ Sitting fees is not included within limits of remuneration
- ✗ In our view, fees may be paid even for passing the resolution by circulation





Change or increase of limits within 11%



✎ Increase of specific limits within 11% is possible with the approval of members by way of special resolution.

For example: Single ED can be paid more than 5% or NED's can be paid for more than 3%





Remuneration beyond 11%



- ✗ Act allows payment of aggregate managerial remuneration beyond 11% without approval of Central Government;
- ✗ Payment of remuneration in case of profits beyond 11% is treated as inadequacy of profit under the Act;

Remuneration of MD/ ED	Net Profits as per Sec. 198	Limits	Adequacy of profits
Rs. 5 crores	Rs. 100 crore	Rs. 5 crores	Adequate (since remuneration is within the limits)
Rs. 5 crores	Rs. 80 crores	Rs. 4 crores	Inadequate





Remuneration beyond 11%



- ✗ For ED: Such payment can be made subject to compliance of Schedule V;
- ✗ For NED: Schedule V doesn't cover NEDs, therefore such payment can be made subject to certain planning.

Note: Companies (Amendment) Bill, 2020, intends to include NEDs (including IDs) within ambit of Schedule V.





Remuneration for Professional Services

- ✗ Remuneration can be paid to any director for providing services, other than what they are bound to render.
- ✗ There are no limits for such remuneration
- ✗ The director should possess the requisite qualification for the practice of the profession.
- ✗ Such remuneration can be paid subject to approval of Board, NRC (if any) and Audit Committee (if any)
- ✗ Such payment of remuneration will also attract provisions of Section 188 with respect to availing of services and office or place of profit





Remuneration for Professional Services

✍ In case of Independent Directors , payment for professional services can't exceed 10% of their total income during a financial year





Approval Mechanism

Within overall limits (11%)	Change in individual limits but within overall limits (11%)
*Nomination and Remuneration Committee (if any)	*Nomination and Remuneration Committee (if any)
Audit Committee (in certain cases)	Audit Committee (in certain cases)
Board of Directors	Board of Directors
Shareholders approval (Ordinary Resolution)	Shareholders' approval (Special Resolution)

****In case of payment of commission to NEDs, approval of NRC will depend upon NRC Policy**





Approval Mechanism-Listed Co (Contd.)

The approval of shareholders by special resolution shall be obtained in the following cases:

- a) Where the annual remuneration payable to a single NED exceeds 50% of the total annual remuneration payable to all NED;



**In case of
Listed
Company**



Special resolution shall be obtained every year

Nature of remuneration	Whether count in the limits under Companies Act	Whether counted in the limits under LODR	Reason
Sitting Fees	No	No	Both the Act and LODR, specifically exclude such fees
Professional Services in any other capacity	No	Yes	Companies Act exclude it specifically but LODR does not.



Approval Mechanism-Listed Co (Contd.)



**In case of
Listed
Company**

b) Where the fees or compensation payable to executive directors who are promoters or members of the promoter group, if:

- ✗ the annual remuneration payable to such executive director exceeds Rs. 5 crore or 2.5% of the net profits of the company, whichever is higher; or
- ✗ there is more than one such director, the aggregate annual remuneration to such directors exceeds 5% of the net profits of the company.

Special resolution shall be valid till the tenure

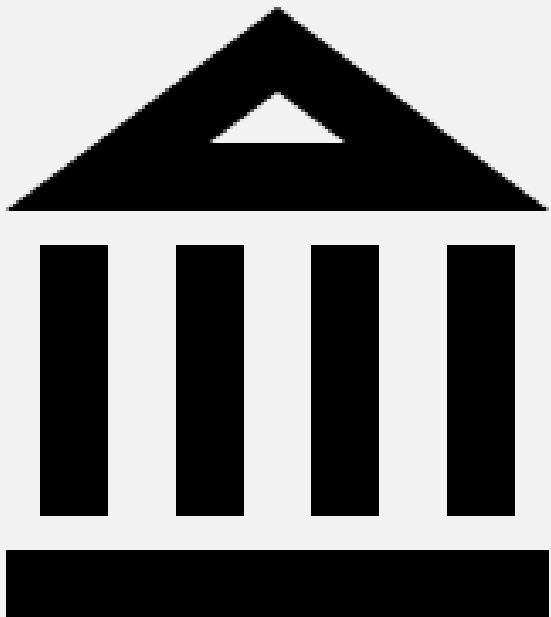


Approval Mechanism (Contd.)

COMPANIES ACT VIS-À-VIS SEBI LODR

Promoter MD/ ED (assuming Net Profit is Rs. 100 crores)	Remuneration	Whether within the limits of Companies Act 2013	Whether within the limits of SEBI LODR on individual basis	Whether within the limits of SEBI LODR on individual basis
MD	Rs. 5 crores (5%)	Yes	Yes	No (since consolidated limit is more than 5%)
WTD	Rs. 5 crores (5%)	Yes	Yes	

Approval Mechanism -Lenders



- ✍ In case of default in payment of dues to any bank or PFI or non-convertible debenture holders or any other secured creditor, the prior approval lender, shall be obtained by the company before obtaining the approval in the general meeting.
- ✍ Whether remuneration can be paid before obtaining approval in case of default?
- ✍ What if default is triggered after shareholders approval: In our view, approval will be required before paying remuneration post default.





Approval Mechanism- Lenders (Contd.)

The RBI vide its notification dated March 27, 2020 and recent notification dated May 23, 2020, has provided moratorium on term loan upto August 31, 2020 secured from the Banks/ Public Financial Institutions. Thus, in case of non-payment of any instalment to the said Lenders during that period does not constitute 'Default'. However, in case of default in re-payment of NCDs or other secured creditors, there is no such exemption.





Managerial Remuneration in form of ESOP



- ✗ In case of ESOP; perquisite arising due on exercise of shares is treated as part of remuneration under the Act due to Income Tax
- ✗ Logically, perquisite on ESOP shouldn't be treated as part of remuneration since it's a notional cost and have no impact on P & L account.
- ✗ At the time of grant of options, perquisites value can't be ascertained , therefore perquisite should be treated as remuneration during the year in which options are exercised.
- ✗ In case of loss or inadequacy requisite compliance should be at the time of exercise





Managerial Remuneration in form of Sweat Equity

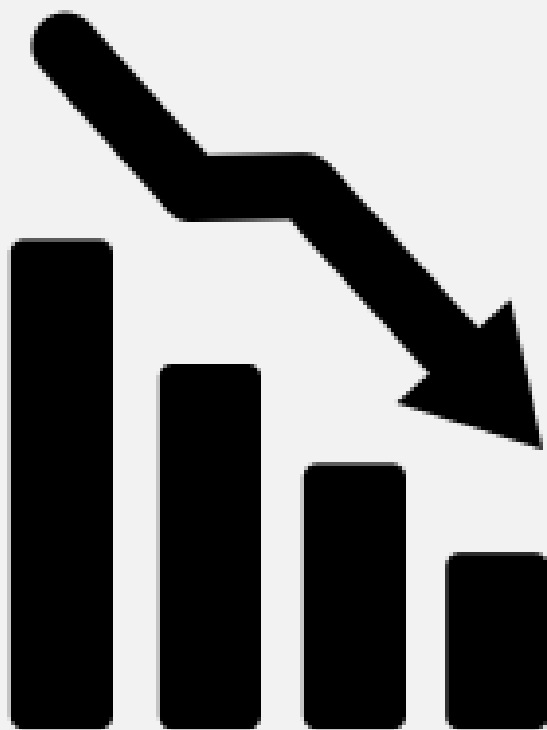


- ✗ Amount of Sweat equity will be considered as a part of managerial remuneration , if such shares are allotted for consideration other than cash and consideration is not in form of asset , which can be recognized;
- ✗ So in case of allotment against cash and any identifiable asset, sweat equity will not form part of remuneration
- ✗ Allotment of Sweat equity , not necessarily be part of terms and conditions of remuneration approved by shareholders for any director.
- ✗ On allotment of sweat equity , limits should be checked and appropriate compliance of Section 197 and Schedule V shall be undertaken.





Schedule V



- Schedule V of the Act provides for the following
 - i) Eligibilities for appointment of ED and Manager
 - ii) Maximum managerial remuneration which can be paid during a financial year
 - iii) In case of loss or inadequacy of profits, situations under which managerial remuneration can be paid and necessary compliances in the said regard

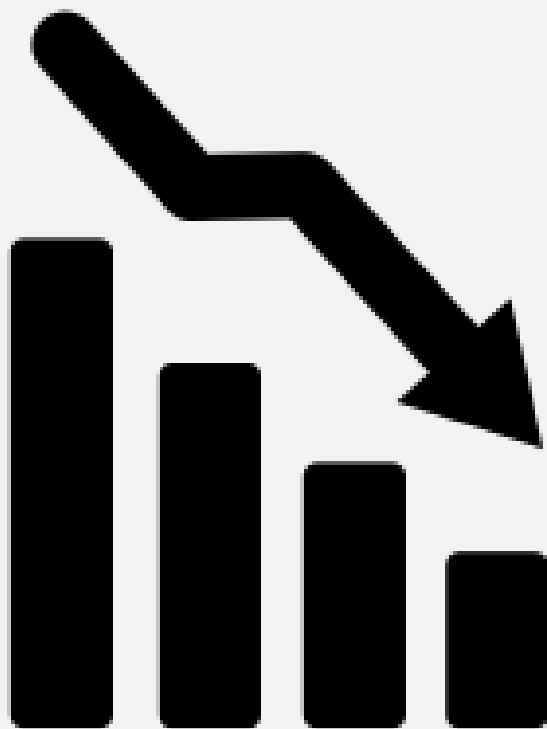




Remuneration to EDs beyond 11% or in case of loss (Contd.)

Situation

- In accordance with limits provided based on effective capital.
- Such limits can be exceeded by passing special resolution



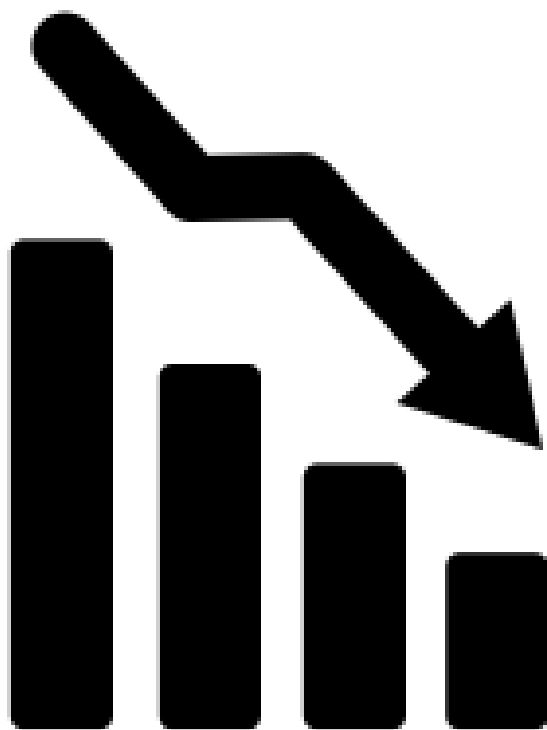
Where the effective capital is	Limit of yearly remuneration payable shall not exceed (Rupees)
Negative or less than 5 crores	60 Lakhs
5 crores and above but less than 100 crores	84 Lakhs
100 crores and above but less than 250 Crores	120 Lakhs
250 crores and above	120 lakhs plus 0.01% of the effective capital in excess of Rs. 250 crores:

- The limits are on individual basis





Remuneration to EDs beyond 11% or in case of loss (Contd.)



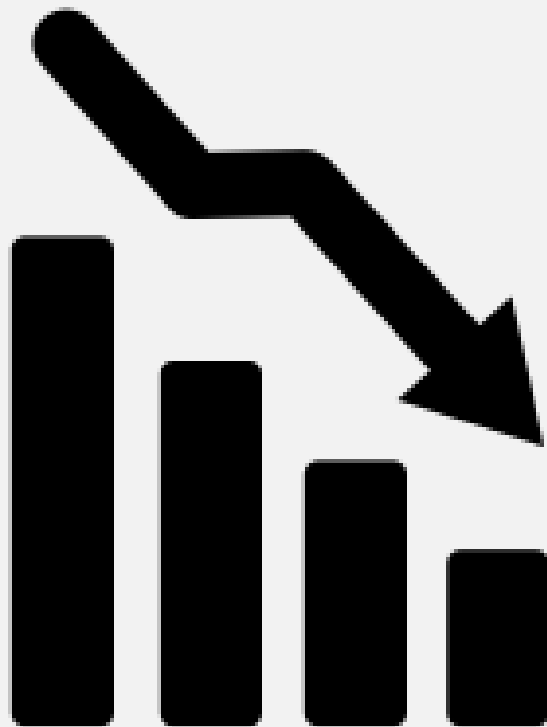
- Effective capital means the
 - ✗ aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long-term loans and deposits repayable after one year (excluding working capital loans, over drafts, 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 investment by an investment company whose principal business is acquisition of shares, stock).





Remuneration to EDs beyond 11% or in case of loss (Contd.)

Situation



- Without any limits to a professional director: where such person
 - ✗ is not having any interest in the capital of the company or its holding company or any of its subsidiaries directly or indirectly or through any other statutory structures (excludes shareholding upto 0.5% pursuant to ESOP) and
 - ✗ not having any direct or indirect interest or related to the directors or promoters of the company or its holding company or any of its subsidiaries at any time during the last two years before or on or after the date of appointment and
 - ✗ possesses graduate level qualification with expertise and specialised knowledge in the field in which the company operates.



Conditions to follow Schedule V

Common



- ✗ Approval of the Board of Directors + approval of the Nomination and Remuneration Committee (if required to constitute);
- ✗ Prior approval of bank/ PFI/ NCDs/ other secured creditor, as the case may be (Where the company has defaulted in payment of such dues);
- ✗ Tenure of remuneration can't exceed 3 years;
- ✗ Disclosure in notice of general meeting





Conditions to follow Schedule V (Contd.)

Specific



Remuneration based on Effective Capital	Ordinary resolution for within limits and special resolution for beyond the limits
Remuneration to Professional Director	Special Resolution





Remuneration to EDs beyond 11% or in case of loss (Contd.)

Other situations, where remuneration beyond limit can be paid

- ✗ Where the remuneration in excess of the limits is paid by any other company and that other company is a foreign company.
- ✗ Where the remuneration in excess of the limits is paid by any other company and that other company has got the approval of its shareholders in general meeting to make such payment, which along with payment to its own managerial persons is within the limits of section 197.
- ✗ Where the company is a newly incorporated company (for a period of 7 years from the date of incorporation).





Remuneration to EDs beyond 11% or in case of loss (Contd.)

Other situations, where remuneration beyond limit is payable

- ✍ Where the company is a sick company for whom a scheme of revival or rehabilitation has been ordered by the BIFR for a period of 5 years from the date of sanction of revival scheme.
- ✍ Where the company is a company in relation to which a resolution plan has been approved by NCLT under IBC, 2016 for a period of 5 years from the date of such approval;
- ✍ Where the remuneration has been fixed by the NCLT.



Conditions to follow Schedule V



- ✍ Ordinary resolution;
- ✍ Except as provided above, the managerial person is not receiving remuneration from any other company;
- ✍ A Certificate from the auditor or CS or CS in practice certifying:
 - that lenders have given no objection for the appointment of the managerial person;
 - that there is no default on payments to any creditors, and all dues to deposit holders are being settled on time.





Key considerations in case of loss or inadequate profits

- ✗ Inadequacy has to be considered with respect to a specific director.

For Example:

Mr. A	5%
Mr. B	5%
Mr. C	5%
Total	15%

Compliance of Schedule V for inadequacy of profits, is not required for all Director and can be obtained for any one of them, since remaining directors are withdrawing within limits

- ✗ Approval in accordance with Schedule V can be obtained either during the financial year or after closure of the year;





Specific points to be considered in case of loss or inadequate profits

- ✗ Following payments will not be considered for limits, in case of inadequacy:
- contribution to provident fund, superannuation fund or annuity fund;
 - gratuity payable at a rate not exceeding half a month's salary for each completed year of service; and
 - encashment of leave at the end of the tenure;
 - Certain allowance in case of expats.





Remuneration to NEDs in case of inadequacy or loss

- ✗ Currently , in case of loss, there is no way to pay remuneration to NED's other than by way of professional services
- ✗ In case of inadequacy of profits, remuneration can still be paid to NED's.
- ✗ In case of inadequacy of profits, keep the remuneration of NED's within the limits of 1% or 3% and take approval for ED's in accordance with Schedule V

For example:

NED's	3%
ED	10%
Total	13%

Remuneration paid is more than 11%, so pay 3% to NED's as per shareholders approval and comply Schedule V for ED's remuneration





Waiver of excess Managerial Remuneration

What is Waiver?



- ✍ If remuneration is not paid in accordance with provisions of the Act, the amount stands recoverable from the Director.
- ✍ Waiver means decision taken by a company to not to recover the unauthorized excess amount.
- ✍ In following cases, waiver of managerial remuneration can be sought:
 - Where requisite approvals for payment were not obtained;
 - In case of loss or inadequacy, where compliance of Schedule V was not undertaken.





Waiver of excess Managerial Remuneration (Contd.)

Approval required



Shareholders Approval

Special Resolution

Lender Approval

Prior approval of bank or PFI or Non-convertible debenture holders or any other secured creditor, in case of default

- ✗ **Time Period:** Within 2 years from the date the sum becomes refundable
- ✗ Amount becomes refundable on signing of audited financial statements.
- ✗ Approval of lender will be required, where there was no default at the time of payment of remuneration but at the time of obtaining waiver approval.
- ✗ Till the date of waiver , excess amount will shown as an recoverable amount in the company's books of account





Managerial Remuneration during FY 2020-21



- ✍ Make an estimation of the financial position for the financial year;
- ✍ In case loss is expected, following can be the ways:
 - Obtain approval of shareholders in forthcoming AGM in compliance of Schedule V; or
 - Go for waiver of remuneration post closure of financial year;
 - Approval will be required for all directors, to whom remuneration is being paid.
- ✍ In case of inadequacy, following can be the ways: :
 - Approval can be obtained in the manner aforesaid or can be obtained through postal ballot at the later part of the year.
 - Obtain approval for only that director(s), on aggregate basis, whose remuneration is expected to exceed limits

Note: Waiver is generally not a good governance practice.





Reduction of Managerial Remuneration



- ✗ Reduction in managerial remuneration, will not require shareholders approval, Board is competent to do so.
- ✗ Approval of NRC and Audit Committee will be required.
- ✗ No approval will be required, if directors are *suo-moto* foregoing their salary.





Modification in Managerial Remuneration



- ✍ Modification in managerial remuneration, so far it doesn't lead to increase, will not require shareholders' approval
- ✍ Board is competent to do so modify the remuneration within overall remuneration
- ✍ Approval of NRC and Audit Committee, will be required.
- ✍ It is advisable to take power to modify remuneration as a part of shareholders resolution



THANK YOU

Nitesh Latwal

Principal Associate
Corporate
Professionals