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Suggestions/ Comments for MCA

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Suggestions/comments as under: -

S.N.	Clause/ Sub-Clause	Suggestion/ Comments	Justification
1	Proposed First Proviso to 149(6)(c) ***i. shall not exceed twenty-five per cent. of his total income,*** *ii. professional or any services rendered by him, shall not **account for more than ten per cent. of his total income.*** ***iii. other than such services, as may be prescribed***	i. The limit of 25% is not practical. Rather than limiting as % of Total Income, the remuneration may be fixed relative to Executive directors/ other IDs / other NEDs remuneration with upper maximum absolute amount if required ii. Other fees may be limited as a maximum % of Board Fee or an absolute amount and in case it exceeds the same then 10% limit must operate. iii. Appear to be a case of drafting error.	**Please see detailed discussion (A, B & C)**
2	Proposed Second Proviso to 149(6)(c)	Only Sitting Fee and reimbursement be included instead of including all fee under 197(5) of the Act.	**Please see detailed discussion (C)**

A: Why proposed limit of 25% total income is not desirable?

On one hand there is a belief that to carry out duties as ID diligently a director must devote enough time to company's affairs and both MCA and SEBI have put limits on maximum directorships as well as committee memberships. Proxy advisors like us have been recommending even lower limits of directorship to ensure that directors do devote sufficient time to board meetings/ committee meetings and prepare for the same.

This suggestion runs contradictory to earlier philosophy. One has to have minimum 5 board positions, which pay almost equally to remain within the limit, assuming that the ID does not have any other source of Income. If for some reason a director resigns from directorship of any company, he has to immediately find another directorship to remain independent on all other 4 boards. This amount to bondage or vitiating independence in other companies whereas the resignation could have come due to independence getting vitiated elsewhere.

This doesn't leave any scope for any individual to have directorships less than 4, if all are equal paying. A proposition that can never be implemented practically or independently. So, one has to take 4+ directorship or none

This will have potential to run contrary to concept of equal work or equal pay, unless the company gets all IDs having same total income.

Or the other course would be that different directors on the same board will earn differently as the cap is not because their contribution to company's board but limited by their total income.

This will not leave any scope for academicians, researchers etc who are not industrialist or top executives of MNC or private companies to become a director. Above issues are best illustrated by following examples;

In fact, the rule will make richer directors richer and would debar entry of others.

Example I

Director A Retired CEO or current CEO of a MNC or Indian Pvt Sector- His annual remuneration is Rs 10 Crore or Pension is 5 Crore

Director B is a retired RBI/ SEBI/IAS/ IRS officer- His maximum annual pension will be Rs 25 lacs (assuming)

Director C is a freelance journalist/ academician- May not be getting pension or total income is Rs 10 lacs/ annum

All three are capable and fit candidates to be director on the company, eminently suited etc.

Company has following options:

1. Pay 25% of annual income as directors' remuneration- this will result in three person doing same work to get paid drastically different amount- Rs 2.5 crore to just 2.5 lac (100 times difference) **obviously this will not work**
2. Pay 25% of the lowest denominator- hence all 3 gets paid 2.5 lacs- bringing socialism – **why A will devote time**?
3. Pay 2.5 lacs to all and compensate Director A by other fees which could run into crore. **This would be bad governance.**

This would not only be impractical but may lead to unforeseen problems. Instead of current proposal following may be considered:

- Fix Maximum absolute amount, if necessary
- Best is to link IDs remuneration at maximum 25% of average remuneration of EDs of the Company
- Ratio of maximum remuneration (all inclusive) to minimum remuneration of IDs not to exceed 2:1
- Similar ratio can be fixed relative to other NEDs (not independent), say at 5:1 meaning NEDs other than IDs may not draw more than 5 times minimum ID remuneration

Example-II

Individual A is an ID in 5 companies say 1,2,3,4 & 5. He doesn't get any fancy pension, all throughout his life he has lived honestly, doesn't even has fancy savings having spent all earnings on education of his children, marriage and building house. Lives on remittances from his kids. Practically no income. But exceptionally capable and doesn't want to dilute his quality and would not want to stretch too much and would be happy to be a director in only 1-2 companies. **Is there any scope for him?**

The answer is **Not at all**

It may be noted that SES had done a study on 'Board Composition and Board Remuneration of NIFTY 500 in India' based on data for 2016-17 for 500 listed companies in association with NSE. Our findings were as under:

Time Commitment of Directors

- In total there are 3,597 unique individuals occupying 4,508 directors' position in the Sample companies.
- Only 171 (4.75%) of individuals have 5 or more listed company directorships. A major chunk i.e. 3,016 (85%) directors have 2 or less number of directorships.
- Most of the persons occupying 5 or more listed directorships are IDs and are above 60 years of age.

Table 1			
Number of Directorships	**Total Positions**	**Individuals**	**Percentage**
1	2,426	2,380	66.17%
2	846	636	17.68%
3	419	254	7.06%
4	326	156	4.34%
5	231	88	2.45%
6	169	57	1.58%
7	64	21	0.58%
8	12	3	0.08%
9	5	1	0.03%
10	10	1	0.03%
Total	4,508	3,597	100.00%

From the above Table, it can be seen that only a handful number have directorships in 5 or more companies. Only 171 (4.75%) of individuals have 5 or more listed company directorships. A major chunk i.e. 3,016 (85%) have 2 or less number of directorships. Further, these 171 persons are having 491 directorships position in the sample. Of these, 371 directorships positions are occupied by individuals who are 60+ years of age, of these 488 directorships position, 381 are IDs and 80 are promoters. It can easily be said that most of the persons occupying 5 or more listed directorships are IDs and are above 60 years of age.

The data clearly shows that there are less than 100 individuals who have more than 5 directorships, indicating that the proposed rule would adversely impact majority of directors and will not be enforceable as many of the directors may not meet total income criteria.

Table 2: Top 10 Directors with maximum directorship in Listed Companies		
S. No.	**Director Name**	**Listed Directorship**
1	Rajendra Ambalal Shah	10
2	Pradip Kumar Khaitan	9
3	Naresh Chandra (*since deceased*)	8
4	Nasser Mukhtar Munjee	8
5	Bansidhar Sunderlal Mehta	8
6	Omkar Goswami	7
7	Dinesh Kumar Mittal	7
8	Murugappan M. Muthiah	7
9	Sanjay Khatau Asher	7
10	Balaji Rao Jagannathrao Doveton	7

The above Table lists out Independent Directors holding maximum directorship in Listed Companies. And, the below Table depicts the remuneration distribution of Independent Directors during FY 2014-15, 2015-16 & 2016-17. The percentage of IDs drawing remuneration above 10 lacs have increased during the 3 years.

Total ID Remuneration (in ₹ lakhs)	No. of Independent Directors				% of IDs		
Table 3	2014-15	2015-16	2016-17		2014-15	2015-16	2016-17
0-5	940	820	743		45.68%	38.30%	34.18%
5-10	376	385	346		18.27%	17.98%	15.92%
10-15	252	304	319		12.24%	14.20%	14.67%
15-50	403	522	644		19.58%	24.38%	29.62%
50-100	55	69	88		2.67%	3.22%	4.05%
100+	32	41	34		1.55%	1.91%	1.56%
Total	2,058	2,141	2,174		100%	100%	100%

From above it is clearly seen that only about 5% directors are getting more than₹ 50 lakhs amount, whereas 95% are below that level. **The proposed rule will adversely impact majority directors.**

B: Why proposed limit of 10% other fee must be linked to total board fee or an absolute limit.

The other fee paid to directors can be for any services. Mainly the services are offered by lawyers, accountants and management consultants. Most of them have flourishing business. Therefore, without absolute limit 10% ceiling doesn't make any sense. For example, a top law firm director can be paid 10% of total income of the concerned partner, which can be a crore or more. Where as an individual brilliant lawyer operating without any firm may not get the same amount although the quality of work could be same/ similar.

One would want this limit to be linked to total remuneration of the director concerned from Company. For example, the limit could be 50% of directors remuneration or an absolute amount whichever is higher.

C: The First proviso states that "*other than such services, as may be prescribed*".

There is a drafting issue and needs to be corrected

Existing Section 197 (5) states that:

> *A director may receive remuneration by way of fee for **attending meetings of the Board or Committee** thereof **or for any other purpose whatsoever as may be decided by the Board**:*

Reading Section 197(5), one understands that a Director can receive remuneration by way of fee for:

- *attending meetings of the Board or Committee*
- ***or for any other purpose whatsoever as may be decided by the Board***

The law also states that such remuneration will not be taken into account for determining pecuniary relationship. By including "***or for any other purpose whatsoever as may be decided by the Board",*** there is a wide-open gate for interpretation.

Further, proposed second Proviso to Sec 149(6)(c) states as under:

> *"Provided further that the remuneration received under **sub-section (5) of section 197** and expenses incurred for participation in the Board and other meetings shall not be accounted for determining the total pecuniary relationship, **unless otherwise provided**."*

Will this amount be included in 10% limit? 25% limit? To remove this interpretation nothing other than sitting fee for board and committee be excluded from limits set and reimbursement of exp for board meetings.

There is a need to reconcile section 197(5) by excluding the words "***or for any other purpose whatsoever as may be decided by the Board",*** as the same has been taken care in section 149 amendments. Appearance of these words in Section 197 not only creates confusion but gives window for different interpretation.

SUGGESTIONS:

Therefore, we suggest that instead of excluding any remuneration received under Section 197(5) the law should categorically provide only for exclusion of fee for attending Board Meetings and Committee Meetings and reimbursement of expenses while arriving at total pecuniary transactions during the period under the proposed second proviso.

Further all payments to director in whatever name or method must be counted for limits undersection 197, else to violate max limit, companies may pay to directors for consultancy contracts.

Profit related commission should not be capped based on Director's total income but should be determined based on objective criteria set for the purpose. Ideally the Company should approach shareholders each year for seeking approval to pay profit related commission for previous Financial Year. This would give opportunity to shareholders to approve commission which appears fair and based on performance of the Directors during the previous year.

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