

# Remuneration for rendering professional services

- CS Gaurav Pingle, Company Secretary, Pune.

Today's corporate world is a world of "Super Specialization", For Example:- If a professional specializes in a domain of Corporate and Securities Laws, now it has become equally important to further specialize into "Corporate Litigation" or "Corporate Restructuring" or "Takeover Code" or "Managing Public Issues" or "Corporate Secretarial Practice" or any other relevant area. Therefore, the saying "Jack of all trades and Master of none" has almost become redundant in this context.

After gaining practical exposure, the professional gains "special" knowledge in a specific domain area and over a period of time, he will be known for his area of practice and expertise in the corporate world. The Corporations prefer appointing such Professionals as Directors in their Company because of their expertise in a specific area, independence and Brand Value in the market. When such Professionals are appointed as Directors in a Company and perform certain duties and assignments which require special expertise, such services are in capacity of a "Consultant" or "Advisors" or "Expert" or "Specialist" or "Practicing Professional".

Many Indian and International Universities offer Specialized and Professional Courses (with research facilities) in the field of engineering, science, management, finance, law and architecture confers Professional Degrees like PhD or Master of Science (M.S or MSc.) after its successful completion.

The provisions of the Companies Act, 1956 ("Act") takes into consideration the abovementioned arrangement between a Specialized Professional (who is a Director) and the Company. The relevant provision is Proviso to Section 309 (1) of the Act. The Section 309 relates to "Remuneration of Directors". The Section 309 (1) states that:-

"The remuneration payable to the directors of a company, including any managing or whole time director, shall be determined, in accordance with and subject to the provisions of Section 198 and this section, either by the articles of the company, or by a resolution or, if the articles so required, by a special resolution, passed by the company in general

meeting and the remuneration payable to any such director determined as aforesaid shall be inclusive of the remuneration payable to such director for services rendered by him in any other capacity:-

*Provided that* any remuneration for services rendered by any such director in any other capacity shall not be so 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) INTERPRETATION OF SECTION 309 (1) AND ITS PROVISO:

The remuneration payable to the Directors (including Managing or Whole Time Director), shall be determined in accordance with and subject to the provisions of Section 198 and 309 of the Act. The remuneration payable to any Director shall be inclusive of the remuneration payable to such Director for the services rendered by him in any other capacity.

The remuneration payable in any other capacity will not be a part of limits prescribed by Section 198 and 309 of the Act, if following Two (2) conditions are satisfied:-

- 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.

Therefore, in order to exclude the amount paid to a Director for services rendered by him in any other capacity; it is necessary to satisfy the two aforesaid Conditions.

The Act has neither defined "Profession" nor "Services of Professional Nature".



The Black's Law Dictionary (5th Edition), defines "Profession" as "A vocation or occupation requiring special, usually advanced, education and skill. The labor involved in a profession is pre dominantly mental or intellectual, rather than physical or manual. The term originally contemplated only theology, law and medicine, but as applications of science and learning are extended to other departments of affairs, other vocations also receive the name, which implies professed attainments in special knowledge as distinguished from mere skill."

**(B) VIEWS OF THE DEPARTMENT OF COMPANY AFFAIRS (NOW, MINISTRY OF CORPORATE AFFAIRS - "MCA"):**

I. In the Tenth Annual Report on the Working and Administration of the Companies Act, 1956 - Year ended 31 March, 1966, it was made clear that:-

"Exemptions under Section 309(1) will be made only in respect of those directors who possess requisite qualifications for practicing the profession in respect of which they render special services."

II. The Department of Company Affairs (DCA), (now, "MCA"), issued a Circular F. No. 6 (8) - CL - VII/67 to define "in any other capacity". It states that:-

"The Amending Act of 1965 has made it clear that Section 309 limited the remuneration of director including remuneration payable to him for services rendered by him "in any other capacity". Hence, the remuneration paid to a director as a partner of the Sole-Selling Agents is for services rendered in "other capacity" and is received by him "directly or indirectly" in excess of the limit prescribed. Hence, prior sanction of the Central Government is necessary.

III. The DCA issued Letter No. 3/54/87-CL-V, dated 14 February, 1988 stating that (relevant part is mentioned):-

- (1) The expression of opinion by the Central Government under the proviso to Section 309 (1) of the Act is required for rendering services by any director, which are of a professional nature. The said proviso is also applicable for practice of the profession as an Advocate as per express provisions made there under.
- (2) The company, in which the Advocate concerned is a director, should apply to the Central Government.
- (3) While making an application, the company should, inter alia state the name (s) of the company (ies) in which the Advocate/Director is a director. The expression of opinion will be required separately for each such director by each such company, is so desired.

(4) Section 309 deals with remuneration of directors individually and not with the firms in which such a director is a partner. The proviso to sub-section (1) refers to services rendered by any director in any professional capacity and, therefore, the question of seeking approval by the Advocates' firms does not arise.

**(C) CRUX OF SOME LANDMARK JUDGMENTS ON "SERVICES RENDERED IN ANY OTHER CAPACITY":**

**I. RAMABE A. THANAWALA V/s JYOTI LIMITED (1957):-**

The Bombay High Court held that "What was sought to be controlled (by Section 309) was the cost of management, and if what was sought to be controlled was the cost of management, then what



had to be considered was managerial remuneration and not remuneration paid for any other purpose. Even on principle this seems to be the correct view, because it is difficult to understand why a company could employ a technical expert and pay him whatever amount it thinks proper and there should be no control with regard to it, and yet the company should be prohibited from making use of the technical knowledge of a director and pay him a proper remuneration."

**II. R. GAC ELECTRODES LTD. AND ANOTHER v. UNION OF INDIA AND OTHERS. (1982):-**

The Kerala High Court held that "The question is whether Section 310 which provides for increase of remuneration has anything to do with the payment of remuneration for Professional Services. The increase can only be an increase of Remuneration. As per Section 309, the remuneration payable to a director takes on only managerial remuneration and remuneration for services of a non-professional nature rendered by him in any other capacity, and remuneration the increase for which permission

*"If you believe you can, you probably can. If you believe you won't, you most assuredly won't. Belief is the ignition switch that gets you off the launching pad." - Denis Waitley*

is required under Section 310 will take in only the above remuneration. As remuneration for services of a professional nature will not be remuneration determined under Section 309(1) the payment of the same to a director will not increase the remuneration he is entitled to under s. 309(1). So, it goes without saying that for the payment of remuneration for services of a professional nature no previous sanction of the Central Govt. under Section 310 is necessary."

### III. RUBY MILLS LIMITED AND ANOTHER v. UNION OF INDIA AND ANOTHER (1984):-

The Bombay High Court held that "It is not the object of the Companies Act to regulate and control the practice or the fees of qualified professionals. That jurisdiction vest elsewhere and, what is more, but for the conditional legislative exception under the proviso to Section 309(1) which, on compliance, exempts Professional Fees and Charges from "Remuneration", the restriction de hors (without) the said proviso may well become unreasonable and absolute in its effect and consequently render itself vulnerable to a constitutional challenges as violating one's fundamental right to practise his profession, merely on becoming a company director simpliciter."

### IV. STUP CONSULTANTS LTD. v. UNION OF INDIA AND ANOTHER (1986):-

The Delhi High Court upheld of the Judgment of "R. Gac Electrodes Ltd" and further stated that "It is not disputed by the Respondents that Section 309(1) enables a company to seek the opinion of the Central Government regarding possession of requisite qualifications, as the provision exists in the Companies Act. Upon the power being invoked

by a company it is necessary and incumbent upon the Central Government, indeed it is its duty, to express an Opinion thereon. The Central Government, cannot side-track the issue by requiring compliance with

another provision, or any other aspect of company law as a pre-condition to the expression of opinion by it."



### V. SREE GAJANANA MOTOR TRANSPORT CO. LTD. AND ANOTHER v. UNION OF INDIA (1991):-

The Karnataka High Court held that "There is nothing in Section 309 of the Act which empowers the Central Government to restrict the remuneration payable to a director for services rendered by him in a professional capacity. Once the Central Government is satisfied that the director possessed the requisite qualifications to render professional services, it is not permissible for the Central Government to put any restriction on the remuneration payable to him by the company in respect of the professional services."

### (D) APPLICABILITY OF SECTION 309:

The provisions of Section 309 of the Act are applicable to Public Companies and Private Limited Companies which are Subsidiaries of Public Limited Company.

Typically, the Non Executive Directors (NEDs) fall under the category of "Super Specialized Director" and any amount paid to NED for obtaining his professional services, in any other capacity, would fall under proviso of Section 309 (1) of the Act.

### (E) OTHER COMPLIANCES:

In this Article, I have focused only on proviso to Section 309 (1) of the Act. But, at the same time we should also take into consideration the other "sister concerned" provisions in the Act i.e. Section 297, 299, 300, 301 and 314. The said Sections along with Section 309 are independent and hence independent compliance is necessary. The disclosures under Accounting Standards - 18 (AS - 18) shall also be taken into consideration along with Accounting Standards Interpretation (ASI) 21 and 23.

For listed companies, it would be desirable to disclose (in accordance with Clause 49 (I) (B) of the Listing Agreement) the Professional Fees paid to NEDs for obtaining their specialized services as a part of good Corporate Governance Practice.

### (F) CONCLUSION:

In the era of "Super Specialization" the provisions of Proviso to Section 309 (1) of the Act are extremely crucial. The need for precise and professional consultancy and services by confidential personnel (i.e. Directors) has become need of the hour. At the same time, we should appreciate the fact that the Act takes into consideration the professional services rendered by directors. The only critical part is that Opinion of the Central Government needs to be sought that Director possesses the requisite qualification.

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*"Its not what happens to you that determines how far you will go in life; it is how you handle what happens to you."*

- Zig Ziglar