

OFFICE OR PLACE OF PROFIT
[Section 314]

For CS/CA Final Students

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Office or Place of Profit

Definition of Office or Place of Profit

As per section 314(3), a director is said to be holding 'Office or Place of Profit' in a company, if he obtains from the company in addition to the remuneration to which he is entitled as a director any salary, fees, commission or any other perquisites while holding the office of a director.

An individual other than a director or any firm, private company or body corporate is said to be holding office or place of profit in a company, if they obtain from the company, by way of remuneration, any salary, fees, commission or any other perquisites while holding the office or place of profit in the company.

Applicability

Section 314 is applicable to both public and private companies.

Office or Place of Profit held by director in the company

As per section 314 certain persons cannot be appointed or allow to hold an office or place of profit in the company unless, they comply with the requirement of the provisions of this section. If any person is proposed to hold such office or place of profit in the company then company has to take consent of the shareholders by passing special resolution in the general meeting of the company.

No such consent is required, if a director receiving remuneration by holding such office or place in subsidiary of the company returned such remuneration to the subsidiary or its holding company.

Scope of the term 'Office or Place of Profit' in a company

The section 314 regulates all such kinds of office or place of profit where any of the persons mentioned therein is required to perform functions on behalf of a company under the control, direction and supervision of the company. In general, there should be employer-employee relationship or that of principal-agent. The person appointed to the office should be required to render duties, services and functions under the instructions of the company concerned. Accordingly, just because some remuneration

like fees or other sums are received from the company, will not make such transactions fall under the prohibition under the section.

The words 'office or place of profit' occurring in section 314(1) include selling and buying agents receiving commission and/or salary. **[CIT v Principal Officer C/o Arkay Wires (P.) Ltd. (2005).**

DCA Clarifications

The DCA has given clarification *vide* **Circular No. 14 of 1975, dated 5-6-1975** to clarify various doubts on the scope of the provisions of section 314(1B) of Companies Act, 1956, as under:—

Section 314 of the Companies Act, 1956, **applies to public as well as private companies**. Sub-section (1) of this section provides that no director of the company and no partner or relative of such director shall hold any office or place of profit, except, that of managing director or manager, banker or trustee for the holders of debentures of the company, carrying a total monthly remuneration of Rs. 500 or more (Old one), under the company unless a special resolution according the consent of the company is passed at the general meeting of the company held for the first time after the holding of such office or place of profit.

The new sub-section (1B) says that notwithstanding anything contained in the aforesaid sub-section (1), no such office or place of profit carrying a monthly remuneration of not less than Rs. 3,000 (Old one) shall be held except with the prior consent of the company by a special resolution and the approval of the Central Government. The proviso to the sub-section (1B) provides that in the case of an appointment to such office of profit having been made prior to the coming into force of the Companies (Amendment) Act, 1974, the approval of the company in general meeting and of the Central Government for holding by such person of the office of profit shall be obtained within a period of six months from the commencement of the Companies (Amendment) Act, 1974.

[Important] A question has been raised whether a special resolution under section 314(1B) is necessary for the appointment of managerial persons who may be relatives of directors and whose appointments are already regulated by section 269, etc. of the Act.

This query arises with reference to public companies to which the said section 269 applies and, strictly, will have to be answered in the affirmative. But in the interests of administrative convenience, it has been decided that the approval of the Central Government once again, under section 314(1B) will not be necessary in the cases

where the Central Government's approval has already been taken under sections 198, 269, 309, 310 and 311, as the case may be. Irrespective of the question of Central Government's approval, the special resolution required under section 314(1B) will have to be passed whether by a public company or a private company.

Another question raised is whether approval of the general meeting and of the Central Government is necessary for an employee drawing salary exceeding Rs. 3,000 per month who is a relative of an existing director but the appointment of such employee was made before his relative became a director *i.e.* whether the exemption under section 314(1A) ensures under section 314(1B) as well. It is considered that sub-section (1) and sub-section (1A) should be read together before applying sub-section (1B) and inasmuch as there is nothing in sub-section (1B) to affect the operation of the principle underlying sub-section (1A), the exemption under sub-section (1A), continues to apply even with reference to a case concurrently falling under sub-section (1B).

In the case of a private company (not governed by section 269, etc. of the Companies Act, 1956) a question has arisen whether the appointment of a person as a managing director who is related to a director of the company will attract the provisions of section 314(1B) where the remuneration payable to such managing director is in excess of the limit envisaged in sub-section (1B). This question is answered in the affirmative. The circumstances that for the purpose of sub-section (1), which deals with appointments to an office of profit carrying less than a total monthly remuneration of Rs. 500 or more (*i.e.* up to Rs. 3,000), an exception is made in respect of an appointment of managing director or manager is not considered relevant because sub-section (1B) expressly overrides sub-section (1) and call for the exercise of a greater vigilance against the likelihood of the abuse of patronage in a case where the remuneration proposed is of the order of Rs. 3,000 per month and more.

A question has also been raised whether provisions of section 314(1B) are applicable where a company proposes to appoint a firm of solicitors and advocates, etc. to help the company in its work. It is considered that an advocate or solicitor appears in a court of law as an officer of the court in pleading the cause of justice and hence, such appearance and receiving fees of that account cannot lead to an inference of an offence or place of profit in or under the company under section 314 of the Act. However, if such a solicitor/advocate, etc. is appointed on a regular retainer basis from rendering legal advice other than appearance in courts, the provisions of section 314 will be applicable.

A question has also been raised whether provisions of section 314(1B) will be applicable to selling arrangements entered into by the company with a partner or relative of directors or with private companies of which such a partner or relative is a director or member. It is considered that these arrangements represent contracts, which fall under section 297 and so far as selling arrangements are concerned they

may also attract section 294AA if the conditions for its operation are attracted; but section 314(1B) is not attracted.

Few cases of appointment of relatives of directors as statutory auditors of the company managed by such directors have come to the notice of the Department. It is conceded that there is no legal bar to such appointments so long as the provisions of section 314 and those relating to appointment of auditor are complied with the appointments are to be regarded as legally valid. It is, however, felt that it would be in the large interests of the profession, if the auditors were to avoid any conflict between their duties as statutory auditors of companies and their personal interest in the management of such companies. As a matter of general principle, a Chartered Accountant, who was a near relation of a director of a company or a partner of a firm in which such director is a partner, should refrain from accepting the appointment of auditor of the company. As regards other categories or relatives of directors, a healthy convention should be established by such persons should not audit or sign the balance sheets of companies managed by their relatives or associates, even though the firms of which they were partners happened to be the auditors of these companies. [Source: Seventh Annual Report on the Working and Administration of the Companies Act, 1956—Year ended 31.03.63]

Circumstances under which a special resolution is required to be passed

As per section 314(1) certain persons as given below cannot hold office or place of profit carrying the remuneration of Rs. 10,000 p.m. or more in the company, unless a special resolution to that effect has been passed in the general meeting of the company:—

1. Any partner of the firm in which director of the company is also a partner;
2. Any relative of a director of the company;
3. Any firm in which a director or his relatives or both are partner;
4. Any private company in which director of the company is holding office of director or member;
5. Any director/manager of a private company in which director of the company is holding office of director or member.

For computing the limit of Rs. 10,000 per month, bonus, leave encashment, reimbursement of medical expenses, etc., which are not events of monthly regularity or occurrence cannot be taken into account.

Where relative of any director or any of the person mentioned above is or appointed to an office or place of profit without the knowledge of director of the company, such appointment shall require the approval of the members in the general meeting by way of special resolution within 3 months of the date of appointment.

Consent of members may be taken subsequently

The appointment of such person under section 314 may be made by the Board at its meeting and may take consent of the company by passing special resolution in a general meeting held for the first time after the said appointment.

However, if the remuneration is more than Rs. 50,000 p.m. (Limit raised from Rs. 20,000 by the Director's Relatives (Office or Place of Profit) Rules, 2003 notified on 5-2-2003) prior approval of members by way of special resolution and the Central Government is required.

Increase in the remuneration of a person appointed in the Office or Place of Profit

If the remuneration of a person appointed in the office or place of profit needs to be increased than the approval of the members of the company by passing special resolution in the general meeting is to be taken, for each time the remuneration is so increased. However, if the appointment is made under time scale in the first instance, there will be no need for further approval of members.

Relative of director or firm in which such relative is a partner, appointed to office or place of profit before a person hold the office of director in a company.

As per section 314(1A) if a relative of a director or firm in which such relative is partner is appointed to office or place of profit in a company before the appointment of such person as a director in the company, it will not effect the continuance of the holding of an office or place of profit by a relative of such director or by a firm in which such a relative is a partner.

Circumstances u/s 314(1) under which special resolution is not applicable

Under the following circumstances, the special resolution shall not be required for appointment of a person on the office or place of profit:—

1. If the monthly remuneration is less than Rs. 10,000 p.m.;
2. If the office or place of profit held by such person(s) in the capacity of managing director/whole-time director/manager/banker/debentureholder trustee;
3. If relative of director has been appointed before becoming director in the company;
4. If director of subsidiary company hold office or place of profit in holding company;
5. If such person is rendering professional advice to the company including director who is consulted or who gives his professional advice to the company occasionally and receive remuneration for such service;

6. If a company purchases or sell materials from or to a director of the company or any of the persons mentioned above to which section 297 will apply. Any person appointed to an office of agent for the sale of the output of the company will be deemed to be holding an office or place of profit under section 314(1).

Circumstances where section 314(1B) is applicable

As per section 314(1B) certain persons as given below cannot hold office or place of profit carrying the remuneration of Rs. 50,000 p.m. or more in the company, unless special resolution to that effect has been passed in the general meeting of the company and **prior approval of the Central Government** has been obtained:—

1. any partner of the firm in which director of the company is also a partner;
2. any relative of a director of the company;
3. any firm in which a director or his relative or both are partner;
4. any private company in which director of the company is holding office of director or member;
5. any director/manager of a private company in which director of the company is holding office of director or member.

Provision of section 314(1B) shall not apply to any appointment of firm of solicitors/advocates, if they are appointed to give advise and are consulted by the company in its work on case to case basis. Therefore, any remuneration or fee received by a professional director as advocates/solicitors for appearing in a Court of Law or Company Law Board/Tribunal in pleading on behalf of the company will not come under the provisions of the section as mentioned above.

Does the appointment of director to the office of secretary also require CG approval?

The Department has instructed that any appointment of director of the company as also its secretary, without any managerial power or *vice versa* shall not require approval of the Central Government. However, special resolution under section 314(1) to that effect is need to be passed if remuneration is in excess of Rs. 10,000 p.m.

Procedure for appointment on office or place of profit, where CG approval required

If a company appoint a director or concerned persons on office or place of profit on a total monthly remuneration of Rs. 50,000 or more, it has to obtain consent of the members of the company by way of special resolution in GM and with the prior approval of the Central Govt. for the first time after the holding of such office. The following procedure has to be complied with:—

1. Hold a Board meeting & consider appointment u/s 314 and approve notice for convening general meeting for passing special resolution by the members.

Explanatory statement with full particulars has to be sent to the members with the notice of the meeting

2. Obtain approval of selection committee (as per rules) for appointment of relative to office or place of profit **before getting approval of members in general meeting;**
3. Hold a general meeting and pass a special resolution for getting approval to the appointment under section 314(1) or (1B);
4. Particulars of such appointment shall be filed with the Registrar of Companies within thirty days of the passing of special resolution in the e-Form 23 u/s 192 alongwith the copy of such resolution and prescribed fees;

5. Prepare and file an application to the Central Government for its approval in the e-Form 24B alongwith prescribed fee;
6. The Central Government may vary the terms and conditions of appointment while according its approval. On obtaining approval from the Central Government, the Company should enter into a contract with the concerned person.

Documents and particulars to be furnished in the application to the Central Government

The following information shall be given in the application:—

- (i) An undertaking from the appointee that he/she will be in the exclusive employment of the company and will not hold a place of profit in any other company.
- (ii) The monetary value of all allowances and perquisites and of total remuneration package (monthly/annually) proposed to be paid to the appointee and details of the services that will be rendered by him to the company.
- (iii) Shareholding pattern particularly the shareholding of the directors along with his/her/their relatives, the public holding, institutional holding (each institution separately).
- (iv) The educational qualification/experience, pay scale, allowances and other benefits of similarly placed executives. In case of the appointment of a relative, then, an undertaking from the director/Company Secretary of the company that the similarly placed employees are getting the comparable salary shall also be enclosed along with the application.
- (v) List/Particulars of all the employees who are in receipt of remuneration of Rs. 50,000 or more per month.
- (vi) The total number of relatives of all the directors either appointed as Managing/Whole-time director, Manager or in any other position in the company; the total remuneration paid to each relative and the total remuneration paid to them altogether as a percentage of profits as calculated for the purpose of section 198 of the Companies Act, 1956.
- (vii) The selection and appointment of a relative of a director for holding office or place of profit in the company shall be approved by adopting the same procedure applicable to non-relatives. However, in the case of public companies, the selection of a relative of director for holding place of office or profit in the company shall have to be also approved by a Selection Committee.

Declaration by a person who is appointed to an office or place of profit

When a person is proposed to be appointed to an office or place of profit, he is required to file a declaration in writing of his connection, if any, with the director of the company as prescribed in section 314(1)/(1B). No declaration need to be filed if the person so appointed is connected to the manager in the company.

Consequences on non-complying with the provisions of section 314

If any office or place of profit is held by certain persons which is not as per the provisions of the section mentioned above then any appointment made under contravention of the section will be held invalid from the date next following the date of holding the general meeting in which the special resolution is passed or from the date of expiry of three months referred to in the second proviso thereunder. Any remuneration received by such persons who were holding the office or place of profit as such shall pay back the remuneration received by them from the company.

The company is not under an obligation to waive the refund of any amount unless the Central Government, on application, waives such refund.

Director's Relatives (Office or Place of Profit) Rules, 2003

1. Short title and commencement.—(1) These rules may be called Director's Relatives (Office or Place of Profit) Rules, 2003.

(2) They shall come into force on the date of their publication in the Official Gazette.

2. Applicability.—These rules shall apply to all companies registered under the Companies Act, 1956 except as provided in these rules.

3. Approval of the Central Government in case of appointment of relatives etc. of directors.—No appointment for an office or place of profit in a company shall take effect unless approved by the Central Government on an application, in respect of—

- (a) Partner or relative of a director or manager; or
- (b) Firm in which such director or manager, or relative of either is a partner; or
- (c) Private company of which such director or manager or relative of either is a director or member, which carries a monthly remuneration exceeding Rs. 50,000 p.m.

4. Procedure of examination of applications.—The application under rule 3 shall be examined with respect to the following, in addition to all other requirements under the Companies Act, 1956: —

- (1) An undertaking from the appointee that he/she will be in the exclusive employment of the company and will not hold a place of profit in any other company.

- (2) The monetary value of all allowances and perquisites and of total remuneration package (monthly/ annually) proposed to be paid to the appointee and details of the services that will be rendered by him to the company.
- (3) Shareholding pattern particularly the shareholding of the directors along with his/her/their relatives, the public holding, institutional holding (each institution separately).

Notification No. GSR 89(E), dated 5th February, 2003.

- (4) The educational qualification/experience, pay scale, allowances and other benefits of similarly placed executives. In case of the appointment of a relative, then, an undertaking from the director/Company Secretary of the company that the similarly placed employees are getting the comparable salary shall also be enclosed along with the application.
- (5) List/Particulars of the employees who are in receipt of remuneration of Rs. 50,000 or more per month.
- (6) The total number of relatives of all the directors either appointed as Managing/Whole time director, Manager or in any other position in the company; the total remuneration paid to each relative and the total remuneration paid to them altogether as a percentage of profits as calculated for the purpose of section 198 of the Companies Act, 1956.
- (7) The selection and appointment of a relative of a director for holding office or place of profit in the company shall be approved by adopting the same procedure applicable to non-relatives. However, in the case of public companies, the selection of a relative of director for holding place of office or profit in the company shall have also to be approved by a Selection Committee.

Explanation.—For the purposes of sub-rule (7) of rule 4, the expression "Selection Committee" means a committee, the majority of which shall consist of independent directors and an expert in the respective field from outside the company.