

Prepared by:

CS Ankur Garg

<https://www.facebook.com/#!/ankur.gargcs>

## **Provisions for Appointment of director by small shareholders at a glance**

Dear Professional Colleagues,

In this article we shall discuss the provisions related to appointment of director elected by small shareholders. This is not a new concept as it was also there in erstwhile Companies Act, 1956 to protect the interests of minority shareholders. Section 252 of the Companies Act, 1956 regulates the process for appointment of director by small shareholders which has now been replaced by section 151 of the Companies Act, 2013.

Companies Act, 2013 has done well to protect the interests of minority shareholders and introduces many favourable provisions in this regard. Appointment of director by small shareholders is a relevant provision in this regard.

### **Meaning of small shareholder**

Small shareholder means a shareholder holding shares of nominal value of not more than 20,000 rupees or such other sum as may be prescribed. A shareholder holding any number of shares up to Rs. 20,000 will be able to participate in the election. Therefore, the market value of shares has no relevance.

### **Old provisions under Companies Act 1956**

Proviso to section 252(1) provides that a public company having paid-up capital of not less than Rs. 5 crore and 1,000 or more small shareholders may have a director elected by such small shareholders in the manner as may be prescribed.

### **New provisions under Companies Act 2013**

Section 151 of the Companies Act, 2013 governs the process for appointment of director by small shareholders. As per Section 151, a listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may be prescribed.

Explanation.—For the purposes of this section "small shareholders" means a shareholder holding shares of nominal value of not more than twenty thousand rupees or such other sum as may be prescribed.

Rule 7 of Companies (Appointment and Qualification of Directors) Rules, 2014, contains detailed process and conditions for Appointment of director by small shareholders.

### **Major Difference between Companies Act 1956 and Companies Act 2013**

Under Companies Act 1956 appointment of director by small shareholders was optional for public companies. In Companies Act 2013 also appointment of director by small shareholders is optional but now it is applicable only on listed companies. This provision is not applicable on private companies and unlisted public companies.

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### **Appointment of small shareholders' Director is optional for Listed Companies**

Rule 7 of Companies (Appointment and Qualification of Directors) Rules, 2014 provides that a company may act *suo moto* to elect a small shareholders' director from amongst small shareholders.

### **Terms and Conditions for appointment of small shareholders' Director**

Please find below point wise provisions for appointment of small shareholders' Director under Rule 7 of Companies (Appointment and Qualification of Directors) Rules, 2014:

1. **Minimum Number of Members required:** A listed company, may upon notice of not less than one thousand small shareholders or one-tenth of the total number of such shareholders, whichever is lower, have a small shareholders' director elected by the small shareholders.

However a listed company may act *suo moto* to elect a small shareholders' director from amongst small shareholders.

2. The small shareholders intending to propose a person as a candidate for the post of small shareholders' director shall leave a notice of their intention with the company at least 14 days before the meeting under their signatures specifying the name, address, shares held and folio number of the person whose name is being proposed for the post of director and of the small shareholders who are proposing such person for the office of director.

#### **Note:**

- a. If the person being proposed does not hold any shares in the company, the details of shares held and folio number need not be specified in the notice.
  - b. A person who is not a shareholder of the company may be nominated by small shareholders for the position of Director under this section.
  - c. Such director shall be considered as an independent director subject to, his being eligible under sub-section (6) of section 149 and his giving a declaration of his independence in accordance with sub-section (7) of section 149 of the Act.
3. The notice shall be accompanied by a statement signed by the person whose name is being proposed for the post of small shareholders' director. This statement must contain the following information:
    - a. Director Identification Number of the nominated person;
    - b. Declaration that he is not disqualified to become a director under the Act; and
    - c. Consent to act as a director of the company
  4. The appointment of small shareholders' director shall be subject to the provisions of section 152 except that-
    - a. such director shall not be liable to retire by rotation;

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- b. such director's tenure as small shareholders' director shall not exceed a period of three consecutive years;
- c. on the expiry of the tenure, such director shall not be eligible for re-appointment.

**5. Disqualification for being appointed as Small Shareholders' Director:** A person shall not be eligible for appointment as a director of a company elected by small shareholders u/s 164, if —

- a. he is of unsound mind and stands so declared by a competent court;
- b. he is an undischarged insolvent;
- c. he has applied to be adjudicated as an insolvent and his application is pending;
- d. he has been convicted by a court of any offence, whether involving moral turpitude or otherwise, 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 expiry of the sentence:  
**Provided** that if a person has been convicted of any offence and sentenced in respect thereof to imprisonment for a period of seven years or more, he shall not be eligible to be appointed as a director in any company;
- e. an order disqualifying him for appointment as a director has been passed by a court or Tribunal and the order is in force;
- f. he has not paid any calls in respect of any shares of the company held by him, whether alone or jointly with others, and six months have elapsed from the last day fixed for the payment of the call;
- g. he has been convicted of the offence dealing with related party transactions under section 188 at any time during the last preceding five years; or

**6. Vacation of office by small shareholders' Director:** A person appointed as small shareholders' director shall vacate the office if-

- a. He incurs any of the disqualifications specified in section 164;
- b. the office of the director becomes vacant in pursuance of section 167;
- c. He ceases to meet the criteria of independence as provided in sub-section (6) of section 149.

**Additional Grounds for vacation of office by small shareholders:** As per section 167, the office of a small shareholders' director shall become vacant in case—

- a. he incurs any of the disqualifications specified in section 164;
- b. he absents himself from all the meetings of the Board of Directors held during a period of twelve months with or without seeking leave of absence of the Board;
- c. he acts in contravention of the provisions of section 184 relating to entering into contracts or arrangements in which he is directly or indirectly interested;
- d. he fails to disclose his interest in any contract or arrangement in which he is directly or indirectly interested, in contravention of the provisions of section 184;
- e. he becomes disqualified by an order of a court or the Tribunal;
- f. he is convicted by a court of any offence, whether involving moral turpitude or otherwise and sentenced in respect thereof to imprisonment for not less than six months;

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**Provided** that the office shall be vacated by the director even if he has filed an appeal against the order of such court;

- g. he is removed in pursuance of the provisions of this Act;
  - h. he, having been appointed a director by virtue of his holding any office or other employment in the holding, subsidiary or associate company, ceases to hold such office or other employment in that company.
7. No person shall hold the position of small shareholders' director in more than two companies at the same time.

Provided that the second company in which he has been appointed shall not be in a business which is competing or is in conflict with the business of the first company.

8. A small shareholders' director shall not, for a period of three years from the date on which he ceases to hold office as a small shareholders' director in a company, be appointed in or be associated with such company in any other capacity, either directly or indirectly.

**Disclaimer:**

This write up is intended to start academic discussion on few significant interpretations under Companies Act, 2013. It is not intended to be a professional advice and should not be relied upon for real time professional facts. Readers are advised to refer relevant provision of law before applying or accepting any of the point mentioned above. Author accepts no responsibility whatsoever and will not be liable for any losses, claims or damages which may arise because of the contents of this write up.

I am hopeful that this write up would be of some help w.r.t. your professional working and endeavors under Companies Act, 2013. Kindly share your opinion.

Thanks

CS Ankur Garg

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