# Positioning the Managing Director Minding his Visa

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*A person who came to India one year ago as a representative of a foreign company to set up a Joint Venture Company for carrying on business in India was issued, being so eligible, a Business Visa for five years. During the last 12 months he has been continuously present in India. According to Schedule XIII to the Companies Act, 1956 he is a resident. He is holding a Business Visa (as opposed to an Employment Visa) which specifically states that, 'Change of Purpose Not Allowed'. Can he be appointed as the MD of the joint venture company in the question probed here.*

A company which is a Joint Venture between a foreign company and an Indian company ('J V Company') is going to appoint one of its foreign Directors as its Managing Director for three years in accordance with the Joint Venture Agreement which formed the J V company one year back. The foreign company has the lion's share in the J V Company as allowed by the applicable sectoral cap under the Foreign Direct Investment Scheme (FDI Scheme) of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000.

The foreign Director who is to be appointed as the Managing Director is the representative of the foreign company and has been in India since the inception and incorporation of the J V Company i.e. a year back.

He was issued a Business Visa immediately before his entry into India by the concerned Indian Embassy in his country, on the basis of the introductory letter of the foreign company and the written representation of the Indian company. Needless to mention, the Indian company (the Indian sponsor in this regard) acted, to comply with the conditions concerning application by a foreigner for Indian Business Visa. The Business Visa is valid for five years with multiple entries.

One year of his directorship with the JV Company has passed. During this period he has stayed in India continuously, obtaining registration from the Registration Officer pursuant to the Registration of Foreigners Act, 1939 (16 of 1939) read with the Registration of Foreigners Rules, 1992.

Schedule XIII to the Companies Act, 1956 ('the Schedule') which stipulates in its Part I the conditions to be fulfilled for the appointment of a Managing or Whole Time Director or Manager without the approval of the Central Government, provides in Paragraph (e) that a managing director should be a person resident in India. For the purpose of this Schedule, resident in India includes a person who has been staying in India for a continuous period of not less than twelve months immediately preceding the date of his appointment as a managerial person and who has come to stay in India,-(*i*) for taking up employment in India, or (*ii*) for carrying on a business or vocation in India. (*Explanation I).*

This condition shall not apply to the companies in Special Economic Zones as notified by Department of Commerce from time to time. (*Explanation II).*

According to the proviso there under, a person, being a non-resident in India shall enter India only after obtaining a proper Employment Visa from the concerned Indian mission abroad. For this purpose, such person shall be required to furnish, along with the visa application form, profile of the company, the principal employer and terms and conditions of such person's appointment.

Thus he fulfills the requirements of Explanation I to Paragraph (e) of Part I of the Schedule and is considered a 'resident in India' as per the Schedule. The Proviso to this Paragraph is an alternative applicable to the person who is considered a 'non-resident' in India and so, not relevant here.

Therefore, the foreign Director can appropriately be appointed as the Managing Director of the J V Company for a period of three years henceforth.

## PASSPORT (ENTRY INTO INDIA) ACT, 1920

According to the Passport (Entry into India) Act, 1920 (34 of 1920) read with Rule 3 of the Passport (Entry into India) Rules, 1950 no person, [excepting some categories of persons given

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under Rule 4 of the Rules] proceeding from any place outside India shall enter, or attempt to enter, India by water, land or air unless, *inter alia*, he is [as per Rule 3(a)] *in possession of a valid passport* conforming to the conditions prescribed in Rule 5.

Rule 5 of the Passport (Entry into India) Rules, 1950 stipulates the conditions of a valid passport. One of such conditions as per sub-Rule (iv) of Rule 5 is quoted below :

> '(iv) that when issued by or on behalf of the Government of a foreign country other than Bangladesh, Nepal and Pakistan , it shall have been *endorsed* by a proper Indian diplomatic, consular or passport authority or by such other authority as may be authorized in this behalf by the Central Government *by way of visa* for India in one or other of the following kinds, namely :
>
> (a) A *single journey visa*, valid for such period not exceeding one year as may be specified therein and for one journey to India;
>
> (b) a *transit visa*, valid for such period not exceeding one year or the period of validity of the visa for the country of ultimate destination, as may be specified therein, and for one or more direct journeys through India undertaken for the sole purpose of reaching any place or country outside India, permitting on each such journey a sojourn of not more than fifteen days in India unless specially extended by a competent authority; and
>
> Provided that in the case of a person entering India over the Tibetan or Bhutanese frontier, it shall also be endorsed by proper Indian diplomatic, consular or passport authority by way of a visa or a transit visa;
>
> (c) an *ordinary visa*, valid for such period not exceeding five years as may be specified therein, and for any number of journeys to India;'

The Passport (Entry into India) Rules, 1950 have been issued pursuant to Section 3 of the Passport (Entry into India) Act, 1920. Sections 4 and 5 of this Act provides for penal conditions for contravention of any Rule / Order under Section 3 as under :

*Section 4: Power of arrest*

(1) Any officer of police, not below the rank of a Sub-Inspector, and any officer of the Customs Department empowered by a general or special order of the Central Government in this behalf *may arrest without warrant* any person who has contravened or against whom a reasonable suspicion exists that he has contravened any rule or order made under Section 3.

(2) Every officer making an arrest under this section shall, without unnecessary delay, take or send the person arrested before a Magistrate having jurisdiction in the case or to the officer-in-charge of the nearest police station and the provisions of Section 1["section 57 of the Code of Criminal Procedure, 1973 (2 of 1974),"], shall, so far as may be, apply in the case of any such arrest.

*Section : 5: Power of removal*

The Central Government may, by general or special order, *direct the removal* of any person from India who in contravention of any rule made under Section 3 prohibiting entry into India without passport, has entered therein, and thereupon any officer of the Government shall have all reasonable powers necessary to enforce such direction.

The conditions of *valid passport* include possession of a *valid visa* [Rule 5 of the Passport (Entry into India) Rules, 1950] which means the conditions against which a visa is issued must be adhered to. *If the conditions of the visa are not complied with, the concerned passport itself becomes invalid and the aforementioned provisions of Sections 4 and 5 of the Passport (Entry into India) Act, 1920 are attracted inviting arrest and deportation of the foreigner.*

The applicant for Indian visa, while making application for visa, undertakes that he shall utilise his visit only for the purpose for which visa has been applied and shall not on arrival in India try to extend his stay for any other purpose.

As given in Rule 5 of the Passport (Entry into India) Rules, 1950, three broad categories of visa is issued on the basis of their purposes, i.e., single journey visa, transit visa and ordinary visa.

Under the aforesaid three broad categories, different nomenclatures of visa are issued denoting the exact purposes, e.g., Employment Visa, Business Visa, Student Visa, Journalist Visa, Transit Visa, Missionaries Visa, Conference Visa, Research Visa etc.

*No Indian Visa can be used other than for the exact purpose for which it has been issued.*

Business Visa falls under 'Ordinary Visa' mentioned in Rule 5(iv)(c) of the Passport (Entry into India) Rules, 1950 .

In respect of Indian Business Visa it should always be kept in mind that –

- It is issued on the basis of :
  - (i) an Indian business house *sponsoring the foreign applicant* and
  - (ii) an organisation of the country of his residence issuing an *introductory letter in his favour.*
- It can be used only for the purpose of 'business' and no other purposes inclusive of 'employment'. The visa itself contains a clear statement on the face of it , '**Change of Purpose Not Allowed**'.

## THE CONFLICTING ASPECT

In the given case, the conflicting aspect lies in the provision of Paragraph (e) of Part I of Schedule XIII to the Companies Act, 1956 as already quoted above.

The person who came to India one year ago as a representative of a foreign company to set up a Joint Venture Company for carrying on business in India was issued, being so eligible, a Business Visa for five years. During the last 12 months he has been continuously present in India. According to Schedule XIII to the Companies Act, 1956 he is a resident in India and can be appointed as the Managing Director of the Company for the next three years. He is holding a Business Visa (as opposed to an Employment Visa) which explicitly states: , 'Change of Purpose Not Allowed'. Does it mean that Schedule XIII to the Companies Act, 1956 ('the Act') does not properly (or knowingly) take into account the conditions under which any visa is issued by the Indian Government to a foreigner ?

The Schedule and for that matter, the Companies Act, 1956 do not make it a compulsion that a Managing Director should be an 'employee' of the company. So, there may be a case that a foreigner can hold a Business Visa and at the same time be appointed the Managing Director of a company.

Again, if that be so [ i.e., the Schedule read with the Act does not contemplate the position of a Managing Director to be an 'employee'] why the provisions of Paragraphs 2 and 3 of Section II of Part II of the Schedule are as below :

'2. A managerial person shall also be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in paragraph 1 of this section :

(*a*) contribution to provident fund, superannuation fund or annuity fund to the extent these either singly or put together are not taxable under the Income-tax Act, 1961,

(*b*) gratuity payable at a rate not exceeding half a month's salary for each completed year of service, and

(*c*) encashment of leave at the end of the tenure.

3. In addition to the perquisites specified in paragraph 2 of this section, an expatriate managerial person (including a non-resident Indian) shall be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in paragraph 1 of this section:

(*a*) *Children's education allowance*: In case of children studying in or outside India, an allowance limited to a maximum of Rs. 5,000 per month per child or actual expenses incurred, whichever is less. Such allowance is admissible upto a maximum of two children.

(*b*) *Holiday passage for children studying outside India/family staying abroad*: Return holiday passage once in a year by economy class or once in two years by first class to children and to the members of the family from the place of their study or stay abroad to India if they are not residing in India with the managerial person.

(*c*) *Leave travel concession*: Return passage for self and family in accordance with the rules specified by the company where it is proposed that the leave be spent in home country instead of anywhere in India'.

Contributions to Provident Fund, Superannuation Fund, Annuity Fund, Gratuity, Encashment of Leave, Children's Education Allowance, Holiday Passage and Leave Travel Concession are attributable to, needless to say, the employee status of a person.

## *Managing Director –Whether or not an 'employee'*

Let us look into some of the relevant provisions of the Companies Act, 1956 in search of the proper status of the Managing Director i.e. whether he is an 'employee' or not :

1. *Definition : Section 2 (26)* **:'** "managing director" means a director who, by virtue of an agreement with the company or of a resolution passed by the company in general meeting or by its Board of directors or, by virtue of its memorandum or articles of association, is entrusted with substantial powers of management which would not otherwise be exercisable by him, and includes a director occupying the position of a managing director, by whatever name called :

Provided that the power to do administrative acts of a routine nature when so authorised by the Board such as the power to affix the common seal of the company to any document or to draw and endorse any cheque on the account of the company in any bank or to draw and endorse any negotiable instrument or to sign any certificate of share or to direct registration of transfer of any share, shall not be deemed to be included within substantial powers of management :

Provided further that a managing director of a company shall exercise his powers subject to the superintendence, control and direction of its Board of directors;'

Thus, he is a Director with the substantial powers of management subject to the superintendence, control and direction of the Board of Directors. This does not suggest that he is under the employment of the company unlike the Whole Time Director.

*Superintendence, control and direction :* This phrase does not necessarily mean **how** the Managing Director accomplishes his responsibilities is subjected to the superintendence, control and direction of the Board . Rather, **what** results he should exactly achieve and when, is so subjected to. Therefore, the Managing Director is not an 'employee' by definition (going by the universally accepted principle to determine the status of an employee).

2. *Certain persons not to be appointed managing directors.: Section 267*

'No company shall, after the commencement of this Act, *appoint or employ*, or continue the appointment or employment of, any person as its managing or whole-time director …….'

The words, 'appointment' and 'employment' have been used by Section 267 as distinct from one another.

3. *Appointment of managing or whole-time director or manager to require Government approval only in certain cases : Section 269*

'(1) On and from the commencement of the Companies (Amendment) Act, 1988, every public company, or a private company which is a subsidiary of a public company, having a paid-up share capital of such sum as may be prescribed, *shall have* a managing or whole-time director or a manager.

(2) On and from the commencement of the Companies (Amendment) Act, 1988, no *appointment* of a person as a managing or whole-time director or a manager in a public company or a private company which is a subsidiary of a public company shall be made except with the approval of the Central Government unless such appointment is made in accordance with the conditions specified in Parts I and II of Schedule XIII (the said Parts being subject to the provisions of Part III of that Schedule) and a return in the prescribed form is filed within ninety days from the date of such appointment.…'

Section 269 all along uses the word, 'appointment' and its sub-Section (1) uses the words 'shall have' in relation to Managing Director.

4. *Number of companies of which one person may be appointed managing director : Section 316*

'(1) [No public company and no private company which is a subsidiary of a public company] shall, after the commencement of this Act, *appoint or employ* any person as managing director, if he is either the managing director or the manager of any other company (including a private company which is not a subsidiary of a public company)], except as provided in sub-section (2).

(2) [A public company or a private company which is a subsidiary of a public company] may *appoint or employ* a person as its managing director, if he is the managing director or manager of one, and of not more than one, [other company (including a private company which is not a subsidiary of a public company] :

Provided that such *appointment or employment* is made or approved by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting and of which meeting, and of the resolution to be moved thereat, specific notice has been given to all the directors then in India. ………'

The words, 'appointment' and 'employment' have been used by Section 316 as distinct from one another.

5. *Schedule XIII :*

Part I of Schedule XIII to the Act begins with 'No person shall be eligible for *appointment* as a managing or whole-time director or a manager ……..'

Paragraph 1 of Part III of Schedule XIII to the Act stipulates, 'The *appointment* and remuneration referred to in Parts I and II of this Schedule shall be subject to approval by a resolution of the shareholders in general meeting'.

In fact, the Act has all along used the word 'appointment' in respect of Managing Director (and also Manager) *either as the only course* (i.e., the word used singly) *or as an alternate course* by dint of which a company 'shall have' (words borrowed from Section 269 of the Act) its Managing Director. But **the Act never uses the word, 'employment' ONLY in relation to 'Managing Director'**.

This implies that the Managing Director has to be 'appointed' but not necessarily 'employed'.

### *Difference between 'appointment' and 'employment':*

According to the Concise Oxford English Dictionary 'appoint' means 'assign a job or role to' and 'employ' means 'give work to (someone) and pay for it'.

According to the Webster's Dictionary 'appoint' means 'charge with a task or function'/'assign a duty, responsibility or obligation to' and 'employ' means 'engage or hire for work'.

According to the Collins Dictionary 'appoint' means 'to assign officially to a job or position' and 'employ' means 'to hire (someone) to do work in return for money'.

### *'Director Simpliciter' to be appointed :*

The Act has used the word 'appointment' in relation to Director Simpliciter (i.e. Director who is not the Managing Director or Whole Time Director) . It has never used the word 'employment' in relation to the Director Simpliciter [ e.g. Vide Sections 257, 260, 262, 263, 264, 265, 266 etc.].

It is absolutely clear that the Act has never intended to give a mandotory status of 'employee' to the Managing Director . On the other hand, the Act qualifies the Whole Time Director (without categorically defining) as 'A director who is either in the whole-time employment of the company……' (sub-Section 3 of Sectio 309 of the Act) and '…… "whole-time director" includes a director in the whole-time employment of the company' (Explanation to Section 269 of the Act).

Certainly, though not intended, but the Act opted for the Manging Director to be an 'employee' which is aptly evidenced in the provisions of Paragraphs 2 and 3 of Section II of Part II of Schedule XIII to the Act as already quoted above.

- From the above discussion the following conclusions emerge :

  1. The Director to be appointed as the Managing Director is a foreigner and holding, along with his passport, a multiple entry Indian Business Visa valid for five years.
  2. He is to be appointed as the Managing Director of an Indian Company for three years.
  3. By virtue of Paragraph (e) of Part I of Schedule XIII to the Act, he is eligible to be appointed as the Managing Director because he fulfills the following conditions-

     (i) He has been staying in India for a continuous period of twelve months immediately preceding the date of his proposed appointment (so, a 'resident in India') as Managing Director.

     (ii) He came to India for carrying on business or vocation (as a representative of the foreign company which is the joint venture partner of the JV Company of which he will become the Managing Director) which justifies his Business Visa.

     [The proviso to Paragraph (e) of Part I of Schedule XIII to the Act calling for 'Employment Visa' is applicable to a 'non-resident' only].
  4. While holding Indian Business Visa he will be appointed the Managing Director of the J V Company according to the provisions of the Companies Act, 1956 read with , precisely, Paragraph (e) of Part I of Schedule XIII to the Act .
  5. One of the conditions of the Business Visa, which is clearly announced on the face of the Business Visa itself, is that '*Change of Purpose Not Allowed*'. This unambiguously denotes that a person holding Business Visa cannot take up any employment in India and if he does so he will do it at his own peril inviting consequences under the Passport (Entry into India) Act, 1920 read with the Passport (Entry into India) Rules, 1950.
  6. The Companies Act, 1956 provides for 'appointment' of Managing Director (as it does so in case of 'Director Simpliciter'). Nowhere the Act makes it mandatory for the Managing Director to be 'employed' (a doctrine not equally applicable in case of a Whole Time Director).

## APPARENT SOLUTION TO THE CONFLICT

The solution to this intriguing state, for the sole purpose of strict compliance with the Passport (Entry into India) Act, 1920 as well as the Companies Act, 1956 may lie in the Agreement of Appointment of the Managing Director suitably providing *inter alia*, that -

- He will be the Managing Director of the J V Company for a period of three years w.e.f.......... but will not be an employee of the Company.
- He will not be entitled to any employee benefits, such as, Provident Fund, Superannuation , Gratuity etc.
- He will be entitled to reimbursement of all expenses including travelling, which he will incur for the company's purposes.
- As remuneration, he wiil be entitled to such percentage of Net Profits of the Company computed in the manner with reference to Section 198 of the Companies Act, 1956 as the Board may decide from time to time during his tenure as the Managing Director within the maximum limit of five percent of such Net Profits [i.e., in compliance with Section 309(3) of the Act].

Following the above, he will be the Managina Director complying with the Companies Act, 1956 without holding any employment taking care of his Business Visa condition.

The above solution is, to repeat, for the sole purpose of striking the balance between the seemingly non-complimentary provisions of the two Acts, i.e., Passport (Entry into India) Act, 1920 and the Companies Act, 1956. It is agreed that the above conditions of appointment of a Managing Director are somewhat uncommon.

As he is the Managing Director payment of commission to him will not fall under sub-section (4) of Section 309 of the Act and consequently, no Special Resolution will be necessary.

## Taxation Angle

The payment of commission should not be taxed under the head 'Salaries' as per section 15 of the Income Tax Act, 1961as there is no employer – employee relationship between the J V Company and the Managing Director and the payment of commission on profit is not his salary.

Whether in such a case *Service Tax* on the services of the Managing Director, who is not an employee as mentioned above, is payable as per Chapter V of the Finance Act, 1994 (as amended from time to time) is debatable. The relevant / nearest taxable service here is the management consultant's service defined in Section 65(21) of the Finance Act as under :

> ' "management consultant" means any person who is engaged in providing any service, either directly or indirectly in connection with the management of any organisation in any manner and includes any person who renders advice, consultancy, or technical assistance relating to conceptualizing, devising, development, modification, rectification or upgradation of any working system of any organization.'

As per the Finance Act the person should be engaged in providing any service, either directly or indirectly, in connection with the management of any organisation in any manner. Under the Companies Act, 1956 the Managing Director has the substantial powers of management. Strictly, providing service *in connection with the management and having himself the substantial powers of management* are not the same.

But, will the Service Tax Authorities ( i.e., the Central Excise Department) consider this finer point especially when the Managing Director is not an 'employee' ! One thing is certain, if his services are considered as 'taxable services', his status as non-employee will get a good support.

Therefore –

- If the foreign Director holds a Business Visa and is a 'resident in India' he is eligible to be appointed as the Managing Director of the Indian Company, in terms of Part I Schedule XIII of the Companies Act, 1956. But, the express conditions exhibited on his Visa [governed by the Passport (Entry into India) Act, 1920] does not entitle him to accept any employment in India . In such circumstances, the only instant solution for him is to be a non-employee Managing Director which may be uncommon but not barred by the Companies Act, 1956.
- Again, if he receives remuneration as Managing Director how he will be treated as non-employee ? Then, remuneration is not the sole criterion to the employee status. If he receives his remuneration only by way of commission on profits, which is well within the scheme of the Companies Act, 1956, his non-employee status can reasonably be supported.
- If he receives 'monthly payment' [vide sub-Section (3) of Section 269 of the Companies Act, 1956] his status as a non-employee may be challenged [even though monthly payment is not the first and last word of employer – employee relationship] at least under the Income Tax Act, 1961 [Section 15].
- His confirmed non-employee status may make his sevices as 'taxable services' for the purposes of the Finance Act, 1994.

## Practical Difficulty

An important question remains : If the Manging Director is remunerated by way of commission on profits and maintains non-employee status by express agreement, not to violate his Business Visa conditions, what happens in the year in which the Company will have no profits?

If the 'minimum remumeration' provisions of Part II of Section II of Schedule XIII to the Companies Act, 1956 are to be adhered to, his non-employee status may face adverse argument.

If, on the other hand, the Central Government's Approval is sought for pursuant to Section 198(4) and / or Schedule XIII to the Companies Act, 1956 for payment of any 'minimum remunreration' to the Managing Director under the given case, the reply letter of the Central Government under the subject matter, 'Approval of of the Central Government under Section 269 & 198(4) / 309(3) and 637AA of the Companies Act, 1956' may, in all likelihood, stipulate the routine condition, '*The expatriate managerial personnel shall come to India on a proper visa i.e., "employment visa"* '.

## THE ULTIMATE OPTION

So, what should be the best solution guarding the finer points of law? Should we agree that the Managing Director be positioned as a 'non-employee' minding his Visa? Will that be the most acceptable solution ? Probably, in the interests of the nation, the principal conditions of an Indian Visa i.e. '**Change of Purpose Not Allowed**' can not be done away with or made flexible. Thus the only other option, is **a suitable amendment to Schedule XIII to the Companies Act, 1956**. ❑