

APPLICATION OF SECTION 203 OF THE COMPANIES ACT, 2013 TO PRIVATE COMPANIES

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ABSTRACT

The Companies Act of 2013 (“Act”) has introduced several new provisions and concepts absent in the previous Act of 1956. One among them is the concept of Key Managerial Personnel (“K.M.P.”). The object of the provision was to bring together a specific group of people responsible for running the company, such as directors, company secretaries, etc. The Act defines K.M.P. to include the Chief Executive Officer (“C.E.O.”) or Managing Directors (“MD”), Company Secretary (“CS”), Whole Time Director (“W.T.D.”), The Chief Financial Officer (“C.F.O.”) and other officers which the Act may prescribe¹. Section 2(51) of the Act covers certain people included in the definition of ‘Key Managerial Personnel. The Act contains several provisions which are related to K.M.P., such as Section 170, which provides that the details of their shareholding must be maintained in a register, Section 179, which mandates the appointment of K.M.P. to be done by the board and Section 184 and 189 which mandates the K.M.P. to disclose their interests. The K.M.P. play a vital role within the company as they are responsible for the day-to-day activities of the company to achieve its target. The members of the board of directors of the company do not generally involve in the day-to-day operations of the company. The board sets out the goals and objectives for the company. The K.M.P. must work on these goals and objectives to be achieved.

SECTION 203 OF THE COMPANIES ACT, 2013

Section 203(1), read with Rule 8 of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, provides a list of companies that must appoint a Whole-time K.M.P. The list includes

- every listed company,
 - every other public company with a paid-up share capital of Rupees 10 crore or more,
- or

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¹ The Companies Act, No. 18 of 2013, §2(51) (Ind.)

- every private company with a paid-up share capital of Rupees 10 crore or more.

Thus, with reference to the above provisions, the Act, along with the rules, provides for a certain threshold or certain companies to comply with the requirement of appointment of K.M.P.

However, a distinction can be seen between the K.M.P., as mentioned in Section 2(51) of the Act, and a Whole-time K.M.P., as mentioned in Section 203. Certain restrictions, such as not holding more than one office, except in a subsidiary, apply only to a whole-time K.M.P. as mentioned under Section 203². In a recent order dated 7th September 2022 in *Hamlin Trust and Ors v LSF10 Rose Investments S.A.R.L. and ors* (“*Hamlin trust case*”), the National Company Law Appellate Tribunal (“N.C.L.A.T.”) has disagreed on the said distinction.

HAMLIN TRUST CASE

The National Company Law Tribunal (“N.C.L.T.”) in a petition filed by L.S.F. 10 Investments S.a.r.l (50% shareholder of Rattan Finance Private Limited (“R.F.P.L.”)/Rose Investments) held that since the Articles of Association (“A.O.A.”) of R.F.P.L. does not provide for any conditions for the appointment of C.F.O. and since the company is a private limited company, any person may be appointed as the C.F.O. although he might not be a full-time employee of R.F.P.L. The A.O.A. stated that the right to appoint the C.F.O. should rest with rose investments. However, the other shareholders shall reserve the right to reject two nominated candidates of L.S.F. and then the third candidate so proposed must be accepted for the post of C.F.O.

The candidates proposed by Rose investments were not full-time employees and were associated with other entities. The remaining shareholders rejected the said nomination on the ground that the appointment was contrary to the procedure mentioned in Section 203 of the Act. The N.C.L.T. directed the appointment of said person as the C.F.O. of the company on the ground that the A.O.A. of R.F.P.L. does not provide for any procedure or criteria for the same.

The N.C.L.A.T., after examining the facts, dismissed the order of N.C.L.T. and held that the provisions of Section 203 should apply to a private company if it voluntarily appoints a C.F.O. since C.F.O. is the K.M.P. of the company as stated in Section 2(51) of the Act. The tribunal further stated that Section 203 states that the whole-time K.M.P. is barred from holding more

² The Companies Act, No. 18 of 2013, §203(3) (Ind.)

than one office other than its subsidiary. Accordingly, the tribunal nullified the appointment of C.F.O. by rose investments.

CONCLUSION

The N.C.L.A.T. order, in this case, has a tremendous impact on companies, mostly private, which confer designations such as C.E.O., C.F.O., etc., without complying with the provisions of the Companies Act, i.e., without filing necessary approvals. This leads to an increase in the number of compliances of the company and may also lead to personal liability at an individual level, as the definition of K.M.P. under the Companies Act is wide enough to include any individual who has been designated as a K.M.P. by the board. Thus, the order has made the definition under Section 203 too wide by applying the same to private companies. Private companies seeking to appoint K.M.P. voluntarily must ensure that they have the necessary approvals mandated under the Companies Act and rules and that all the provisions relating to K.M.P. are strictly adhered to.

