

## Role and liabilities of Director to a Company

### 1) Definition of Director

As per section 2(34) of the Company Act, 2013 "Director" means a Director appointed in Board of Company.

### 2) Person eligible to be appointed as as Director

An individual is eligible to be appointed as Director unless:

- ★ **Declaration of Unsound Mind** by the competent court
- ★ **Undischarged insolvent** or pending application for insolvency procedure.
- ★ **Convicted and punished** with imprisonment not less than six months **for an offence involving Moral Turpitude.**
- ★ **Declared by the tribunal or other competent court disqualified** to hold the position of Director
- ★ **Appointed** as such **without having DIN**
- ★ Holder of such position in more than twenty company at a time in contravention to section 165 of the company law.
- ★ **Disqualified due to non filing of DIR-3 KYC** on MCA official site.
- ★ Holding such position in a company, which has not filed ACTIVE Form (INC-22A).
- ★ **Failed in filing financial statement or annual return** for continuous period of 3 financial years.
- ★ **Disqualified on account of non-return of deposits or Non-payment of dividend** under section 164(2) of the Company Act 2013

### 3) Company as an independent corporate person

#### Seperate legal entity

- The house of lord in a very famous case **Salomon Vs Salomon UKHL 1, [1897] AC 22** held that a company is a separate legal entity isolated from its members.
- This principle is also known as '**veil of incorporation**' means as a corporate person a company had its own existence, rights and liabilities distinct from its members.

### 4) Liabilities of Director as an agent or officer of company

To look upon whether a Director to a company is discharging his duties for the welfare or benefit of shareholders, member or creditors or not the judiciary use the principal of lifting of corporate veil. To make the Director liable for his fraudulent, misconduct or dishonest act various provisions have been included in the Company Act, 2013.

## Lifting of corporate veil

- The fraudulent and dishonest use of body corporate for personal benefit and against the interest of shareholders or members to company can be a primary cause the court resorts the principal of lifting of corporate veil to see who are in full control of company to check on fraudulent and dishonest acts.
- The court in a famous case **United States V. Milwaukee Refrigerator Co., [1905] 142 F 242** held that a corporation will be looked upon as a legal entity as a general rule.....but when the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud or defend crime, the law will regard the corporation as an association of persons.”
- The court in **Cotton Corporation of India Ltd. v. G.C. Odusumath ILR 1998 KAR 2553, 1998** laid down the rule that the courts can lift corporate veil only when provisions for the same is expressly provided within the statute.
- The Hon'ble Delhi High Court in **Sudhir Gopi v. Indira Gandhi National Open University, 2017 SCC OnLine Del 8345** held that mere failure of a corporate entity to meet its contractual obligations is no ground for piercing the corporate veil. In this case the court observed that Arbitral Tribunal cannot bind other parties who have not agreed to arbitrate,
- There are two types of provisions for the lifting of the Corporate Veil-  
a) Judicial Provisions and b) Statutory Provisions

### 4.1 Fiduciary liability of Director towards company and it's shareholders or creditors

The concept of Fiduciary Duty/Liabilities, although not specifically defined, is enshrined in the Section 166 of the Company Act, 2013. This provisions imposes statutory obligation upon the Director of a company that he will perform following duties as a trustee or officer to company:

- ★ Duty to comply with Article of Association to company.
- ★ Duty to act in good faith and in the interest of shareholders.  
The good faith would require that all the endeavours of the directors must be directed to the benefit of the company. (**Bank of Poona Ltd v. Narayandas , AIR 1961 Bom 252 at 253**).
- ★ Duty to exercise reasonable care, skill and diligence.
- ★ Duty to avoid conflict of interest
- ★ Duty not to accept undue gain and advantage.
- ★ Duty not to transfer directorship in favor of other person.
- The court in **Great Eastern Railway Company v. Turner, 1872** observed that “the **Directors are the mere trustees or agents of the company**—trustees of the company’s

assesses, agents in the transactions which they enter into on behalf of the company.” Directors are not employees of the company, but persons responsible for the conduct of its affairs, **and act in a fiduciary capacity.**

- The court in **Albert Judah Judah vs. Rampada Gupta and Ors., AIR 1959 Cal 715**, observed that Director may be made liable “**for breach of trust when he misapplies the fund and misappropriated any assets to company.**”
- The Supreme Court in the case of **Official Liquidator v. P.A. Tendolkar {1973} 43 Com cases 382**, held that a director could be held liable for dereliction of duties if his negligence is of such character as to enable frauds to be committed and losses thereby incurred by the company.

**4.2 Personal Liabilities of Director regarding Non-payment of Debt:** The Director to a company can be made personally liable for following acts:

- ★ False statement in company prospectus
- ★ Fail to file disclosure under the SEBI Rules and Regulations
- ★ Fraudulent Business conduct
- ★ Failed to pay qualified shares
- ★ Fails to share application money payment (during placement of share offer)
- ★ Company Debt
- ★ Liability to file tax return within prescribed time.
- The Hon'ble Gujarat high court in **Satellite Television Asian Region Ltd. and Ors. vs. Kunvar Ajay Designer Saree P. Ltd. 2003** held that even winding up procedure doesn't absolve the Director from criminal liability if he continues carry on business exploiting his position as a trustee of a company and incurs debt to creditors with intention to just defraud the creditors.
- The Apex court in **K. Srikanth Singh v. North East Securities Ltd. 2007** held that the Director of a company does not become automatically liable for offence committed on behalf of the company, and it is necessary to make specific averments in this respect
- The Delhi high court in **Alibaba Nabibasha Vs. Small Farmers Agree-business Consortium & Ors. 2020 SCC OnLine Del 1250** stated that a person who has retired as the director of the company can't be held liable for the day to day acts of company and cheques issued and dishonoured post-retirement.

### **4.3 Vicarious Liability**

Vicarious liability is a concept under which a person is liable for an act committed by other person. Corporate criminal liability is a crime committed by an individual or group of individuals connected with a company (directly or indirectly), who for purpose of gain undue advantage or

unjust enrichment commit an act forbidden by law. The concept of vicarious liability is evolving and explained by various courts time to time.

- The Supreme Court in the case of **“Sunil Bharti Mittal v. Central Bureau of Investigation” AIR 2015 SC 923** held that the concept of ‘vicarious liability’ is unknown to criminal law. Statutes must expressly and indisputably contain provisions attaching such vicarious liability. It is obligatory on part of the complainant to make specific allegations against the Directors in order to make them vicariously liable.
- The apex court in **SEBI v. Gaurav Varshney, 2016 14 SCC 430** held that liability arises from being in charge of and responsible for the conduct of the business of the company at the relevant time when the offence was committed and not on the basis of merely holding a designation or office in a company.
- The apex court in **SEBI v. Gaurav Varshney, 2016 14 SCC 430** held that liability arises from being in charge of and responsible for the conduct of the business of the company at the relevant time when the offence was committed and not on the basis of merely holding a designation or office in a company.
- The Hon’ble Supreme Court in **Shiv Kumar Jatia v. State of NCT of Delhi Criminal Appeal No. 1264 of 2019** has rightly held that allegations against a director which are vague in nature and which do not attribute any intent for commission of an alleged offence to the director, do not constitute a prosecutable offence against the director, even though the company and its other employees may be held liable for the very same offence.
- The court in **Shailendra Swarup v. Enforcement Directorate, 2020 221 CompCas 758 (SC)** held that Vicarious liability cannot be imposed on any director in the absence of legislative mandate.
  - ✓ The Ministry of Corporate Affairs (“MCA”) has vide its March 2020 circular issued directions to the **Registrar of Companies**, directing them **not to initiate any civil or criminal proceedings against Independent Director or Non Executive Directors (non-promoters and non-Key Managerial Person like C.E.O, C.F.O and M.D) unless sufficient evidence exists against them.**