



## Compliances with Companies Act, 2013 – Part IV

*This write up provides an overview of some of the important changes with respect duties and liabilities of directors under the new Companies Act.*

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### ***Duties and Liabilities of Directors***

The institution of board of directors plays a prominent role in corporate governance. It is responsible for directing and overseeing the business and management of the company. Given this vital role of the board, directors are considered as fiduciaries in that they are required to act in the interest of the company as well as various constituencies in a company such as shareholders and other stakeholders. Accordingly, the law imposes directors with duties and liabilities as tools that regulate their conduct.

Until the coming into effect of the Companies Act, 2013 (the “Act” or the “Companies Act”), these duties and responsibilities were largely uncodified and directors were to perform their fiduciary duty towards the Company and its shareholders. The new Companies Act provides for specific duties and liabilities of directors.

### ***Duties Of Directors***

Section 166 of the Companies Act provides certain duties of directors, which are as follows:

<b>Due care, skill and diligence</b>		
1.	<b>Comply with Charter Documents</b>	A director shall always act in accordance with articles of association of a company.
2.	<b>Alignment with Objects of the Company</b>	A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, and the community and for the protection of environment.
3.	<b>Due and reasonable care</b>	A director of a company shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment i.e. not be swayed towards the management or any one shareholder.
<b>Fiduciary Duties</b>		
4.	<b>No Conflicts</b>	A director of a company shall not be involved in a situation in which he may have a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the company.
5.	<b>No undue advantage</b>	A director of a company shall not achieve or



		attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates
6.	<b>No assignment</b>	A director of a company shall not assign his office and any assignment so made shall be void.

### *Consequence of Contravention*

Where a director contravenes the provisions of Section 6 i.e. fails to perform the duties cast on him, such director shall be punishable with fine which shall be not less than INR 1,00,000 but which may extend to INR 5,00,000.

### *Independent Directors*

While imposing the above duties on directors, special provisions have been made to the duties, roles and functions of independent directors under Schedule IV.

Independent directors in addition to the above duties applicable to all directors shall be further required to fulfil the following functions in respect of a Company:

- 1) Following the guidelines of professional conduct. The guidelines include upholding ethical standards of integrity and probity, exercising his responsibilities in a bonafide manner in the interests of the company, at all times be objective in their thinking, no abuse of position etc.
- 2) Bring independent judgement to the board including on issues of strategic importance, performance risk management as well as key appointments etc.
- 3) Scrutinize performance of management.
- 4) Review internal financial controls and be satisfied on the integrity of the financial information.
- 5) Safeguard interests of all stakeholders including minority shareholders.
- 6) Balance conflicting interests of all stakeholders (environment, shareholders and community at large).
- 7) Remuneration of key executives
- 8) Assume the functions of a moderator where there is a conflict between management and shareholders.

The duties of an independent director are provided in **Annexure 1**.

### *Liabilities Of Directors*

Given the number of duties specifically hoisted on directors, the Act also provides specific liabilities on the directors, which we can term “**statutory liabilities**”.

Statutory liabilities may be divided into:

- Civil liabilities (requiring directors to make payments to victims or the state) or criminal liability (resulting in fines or imprisonment).
- The approach in the new regime has been to impose stiffer penalties in case of a criminal offence so as to constitute a strong deterrent on director conduct that falls short of the desired standards.



Examples of statutory liability are set out below:

- 1) Liability for misstatements in prospectus (sections 34 & 35). Certain directors including promoters and experts shall be personally liable for any loss caused to any person who subscribed to the prospectus;
- 2) Imposition of fines for breach of directors' duties (section 166);
- 3) Prosecution for fraudulent trading (section 339). Every director shall be personally responsible without any limitation for all debts and other liabilities of a company as the Tribunal may direct; and
- 4) Fines in the case of offences where no specific punishment is prescribed (section 450).

### *Shareholder / Company Claims*

It is possible that claims may be made against the directors either by the company or the shareholders for breaches of directors' duties. Since directors owe the duties to the company, at the outset it is the company that can bring a claim. Where the company is unable (or does not wish) to do so, it is open to the shareholders to bring a derivative claim on behalf of the company to recover monies for breach of directors' duties.

### *The Silver Lining*

There are several mitigating factors that would assist a responsible director to respond to claims made against such director. Some of these factors are set out below.

Relief of independent / non-executive directors: Section 149(12) provides that notwithstanding anything contained in this Act (i) an independent director and (ii) a non-executive director not being promoter or key managerial personnel, shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

No restriction on indemnities or D&O: Directors may obtain indemnities from the company, which was specifically prohibited under the earlier Act. Directors hitherto could not be indemnified for negligence, default, breach of duty and the like. The Act, however, does not contain such a restriction. Directors may seek indemnities from the company in case they have to meet any liabilities, particularly if no fault can be attached to the directors' conduct. The Act also imposes no restrictions on obtaining Directors and Officers liability insurance. This practice may be continued.



## ANNEXURE 1

### DUTIES OF INDEPENDENT DIRECTORS

Independent directors shall:

1. undertake appropriate induction and regularly update and refresh their skills, knowledge and familiarity with the company;
2. seek appropriate clarification or amplification of information and, where necessary, take and follow appropriate professional advice and opinion of outside experts at the expense of the company;
3. strive to attend all meetings of the Board of Directors and of the Board committees of which he is a member;
4. participate constructively and actively in the committees of the Board in which they are chairpersons or members;
5. strive to attend the general meetings of the company;
6. where they have concerns about the running of the company or a proposed action, ensure that these are addressed by the Board and, to the extent that they are not resolved, insist that their concerns are recorded in the minutes of the Board meeting;
7. keep themselves well informed about the company and the external environment in which the Company operates;
8. not to unfairly obstruct the functioning of an otherwise proper Board or committee of the Board;
9. pay sufficient attention and ensure that adequate deliberations are held before approving related party transactions and assure themselves that the same are in the interest of the company;
10. ascertain and ensure that the company has an adequate and functional vigil mechanism and to ensure that the interests of a person who uses such mechanism are not prejudicially affected on account of such use;
11. report concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct or ethics policy;
12. acting within his authority, assist in protecting the legitimate interests of the company, shareholders and its employees;
13. not disclose confidential information, including commercial secrets, technologies, advertising and sales promotion plans, unpublished price sensitive information, unless the Board expressly approves such disclosure or required by law.