

Pitfalls and Safeguards in the Obligations of Directors under Indian Companies Act 2013

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ABSTRACT

Directors must be well aware that as company's directors they are individually subjected to legal duties in their capacities. Additionally, the companies are autonomous legal entities subjected to legal controls as well as it has been ensured by the directors that these legal controls are compiled by the companies. A company's commercial success within the regulatory framework depends on an individual that manages the company, therefore, it is essential that individual as a director must be fully aware of his responsibilities as well as guidelines and principles' appropriate management knowledge. A corporation's management is dealt by the corporate governance. Various strategies controls and guides businesses within the permitted legal and regulatory framework. A company is ultimately led by the Board of Directors for its stakeholders' good. This deals with balancing social and economic goals, societal and individual objectives. The Directors must also be aware of the pitfalls, if they are not acting in accordance with the reasonable expectation from their position. The aim of this paper is to study the pitfalls and safeguards under the Indian Companies Act 2013 in discharging the responsibilities of directors.

Keywords: Corporate, Compliance, Governance, Pitfalls, Safeguards, Directors, Companies, Indian companies.

I INTRODUCTION

In view of the modern scams in Indian corporate landscapes as well as numerous directors' prosecution, for the directors it is essential in Indian regulatory set-up to evidently understand their duties and responsibilities as directors. Furthermore, for the directors it will be practical for determining their efforts as well as responsibilities at preventing the risks having peaceful time as director, for contributing more efficiently in the company, economy as well as the country's growth at large. While the structure of corporate governance may vary from organization to organization, most companies incorporate the key elements including, all shareholders will receive fair and equal treatments. This includes guaranteeing that shareholders are aware of their responsibilities as well as how these are implemented. It is essential for upholding social, contractual and legal responsibilities to non-shareholder stakeholder. It also involves the exchange of relevant information to staff, customers, and group suppliers. The Board of Directors should preserve a commitment for ensuring transparency, fairness and accountability of corporate governance. The members of the board must also have the requisite expertise to review management activities. Directors of a company are essentially trustee operators owe obligations towards shareholders, investors and government. In this way, the Directors play an exceptionally critical role in any corporate governance system.

Recent times' main corporate scams such as Satyam Computers, Sahara, and Kingfisher have many times shown the inabilities in the earlier corporate legal framework to be ineffective in upholding Corporate Governance. In most of such cases Directors are responsible for breaking expectations of shareholders

as well as sometimes not respecting the shareholders' sentiments under an allure' false veil, whereas for fulfilling the personal welfare corporate mechanism is utilized. After the last amendment's approximately 50 years, Companies Act 2013 has been passed for meeting such challenges. This act developed on principles of openness and self-regulation through disclosures, shareholders' protection of interests, and Board's responsibility. Various effective controls are ensured by the 2013 amendment as Directors' responsibilities and liabilities are clearly defined as well as on failure penal actions are followed. The purpose of this paper is to study the Pitfalls and Safeguards in Directors' Obligations under the Indian Companies Act 2013.

II DIRECTOR IN A COMPANY

(a) **Directors' Role in a Company-** Companies Act, 2013, Section 2(34) describes a director as – “director” means a director selected for the company's Board. A Director is critical component for an aggregate body known as the “Board of Directors”, liable for the organization's undertakings' oversight, control, as well as heading. Accountability is a very important aspect of Board effectiveness. There are internal and external mechanisms for assessing the directors' ongoing performance. But a director's liability primarily depends on his or her directorship's nature. In application of corporate governance's general principles, broadly four principles have developed. These are (1) directors must avoid the conflict of interest (2) that they must not hamper their discretion as to how they must act (3) for purposes they must exercise powers for those that they are conferred and (4) that they must act

in good faith in what they deem to be the in the best interest of the company.

(b) Director’s Legal Position- In any corporate enterprise, the position of a director cannot be explained easily (“Ram Chand & Sons Sugar Mills Pvt. Ltd.vs. Kanhayalal BhargavaAIR (1996) Cal”). L.J. Bowen gave the director position in “Imperial Hydropathic Hotel Co Blackpool v. Hampson” case ((1883) 23 Ch D 1) in a corporate organization the director has an adaptable position. Also, directors are defined as agents, or as trustees as well as sometime as managing partners. So the question that arises is what is the director’s position in the company whether he is an agent or a trustee? Considering directors as a servant of the company will be wrong as these are professional men and women of the company that are employed for directing the company’s affairs. A more satisfactory way to describe them is as company’s officers. Furthermore, in “Moriarty v. Regent’s Garage Co”case ((1921) 1 KB 423), it has been stated

that a director is not company’s servant rather he is company’s activities controller.

It was believed that directors are company’s agents as it is considered as artificial person that acts through directors only (Ferguson v. Wilson (1904) SLR 41 601). The relation of a director as well as the company is considered as agent and principal’s an ordinary relation. Directors are not the company’s trustees, however they are considered as trustees where money properties and money are involved as it is under their control. In “Ramaswamy Iyer v. Brahamayya & Co.” case (AIR (1965) Mad 176), it was held that the directors are responsible as trustees in terms of their company’s power of using funds as well as for power misuse, as well as even after their death the liability remains as an action cause exists contrary to their legal representative. Directors can be described as trustees due to their office nature as Directors are employed for managing the company’s affairs for shareholders’ advantage. The company’s director cannot be considered as a trustee in his true form as a marriage or will settlement trustee. As the director of the company is company’s paid officer.

<p>(a) Directors as Agents : An organization acts as a counterfeit individual through directors who are chosen delegates of investors and who settle on choices for investor advantage.</p>	<p>(b) Directors as employees In case the director is employed as the company's full-time employee, the specific directors are considered to be full-time director or employee director.</p>	<p>(c) Directors as officers In case the director is considered as a company officer. On the off chance that the business act arrangements are not carefully agreed with, they are obligated for certain punishments.</p> <p>• Manager as Trustees:</p> <p>The Directors will be considered as trustees of property, cash and business: as well as just as forces’ trustees provided to them as well as vested in them.</p>
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(c) Director as “Officer”
“Officer” means a manager, director or significant managerial staff, or an individual who is or is familiar to acting according to Board of Directors or of any or more of the directors’ instructions or directions.

(d) Director as "Key Managerial Staff"
“Key managerial personnel” means “key managerial staff” with respect to a business.

- (i) The Manager or the Director General or the Chief Executive Officer;
- (ii) the Chief Financial Officer;
- (iii) the Chief Financial Officer;
- (iv) the director for the whole time;
- (v) the company’s secretary; and
- (vi) the other officer, as may be specified;

(e) Director as “Officer In Default”
“Officer who is in default” signifies, for the reasons for an arrangement in the particular Act, any of the following officers of an organization which expresses that an officer of an organization who is in default is obligated for any punishment or discipline via detainment, fine or otherwise, in other words, fine or otherwise:

- (a) Director for the entire time;
- (b) On the off chance that, as indicated by the Board in that name, there are no key administrative staff, for example, the chief or directors, who have, or have given, the composed assent of the Board or all the directors to that detail, given that no chief has determined it;
- (c) Key chief faculty;
- (d) Any individual who is acquainted with acting in agreement with the guidance, course or heading of the organization's Board of Directors, other

than the individual who exhorts the Board in a professional limit;

- (e) Any individual that, under any significant administrative staff's or the Board quick authority, is subject for any obligation, including the safeguarding, filing or conveyance of records or records, approves, takes an interest actively, knowingly approves or knowingly neglects to find a way to maintain a strategic distance from any default;
- (f) for the issuance or move of any offers in an organization, for the issuance or move by share move specialists, enlistment centers, and shipper brokers of any offers in an organization;
- (g) Any chief who, in break of any of the arrangements of this Act, knows about such an infringement on the ground that the Board has gotten or taken an interest in any proceedings without objecting to it, or who has submitted such an infringement with his assent or intrigue;

As there does not exist a body or mind in a corporation of its own and its actions are performed by an individual that is not just a trustee or agent however, by somebody the company will be responsible since that individual's actions are the company's action itself. In case a company is considered as a human body, then one can consider director as company's will and mind as company's actions are controlled by them. As discussed above position of a director is complicated one even though a director cannot be called a servant of the company it is called the officer or the controller of the company. Similarly, the director is not the trustee of the company he is a trustee in respect of money and property and the trustee of the company not of the shareholders. In true sense, the directors are the agent of the company and have a relationship as an agent and principal. Lastly, the director is the brain of the company.

(f) Duties and Responsibilities Of Directors

The Director is essential for the Board, the aggregate of Directors, which is answerable for overseeing, controlling and directing the undertakings of the organization. Traditionally, the obligations of the Directors are to a great extent got from organization and trust law, according to customary law rules and reasonable principles (that is, non-contractual, semi contractual and contractual guardian associations set with the Company). Ability, care and perseverance of obligations are forced on directors according to the law of the association. Trust laws, then again, force guardian duties upon directors.

III PROVISIONS OF COMPANIES ACT

(a) Obligations on a Director

According to Indian Companies Act, 2013, Section 166 following obligations are put on Directors:

- (i) A Company's Director shall not assign his office as well as any assignments made shall be void.
- (ii) Unpublished price to be maintained, technologies, commercial secrets, sensitive proprietary information's confidentiality must not be disclosed until it is required by law or board approved it.
- (iii) To ensure users as well as company's vigil mechanism are not affected prejudicially on such usage account.
- (iv) The Director must ensure that adequate deliberations are held before approving related party transactions as well as these transactions are in the company's interest.
- (v) A director should always be aware of conflict of interest situations and should try and avoid these conflicts for the company's interest.
- (vi) A director shall use independent judgement for exercising his responsibilities with reasonable and due diligence, skill and care.
- (vii) A director must follow company's stake holders' the best interests, in good faith as well as for promoting the company's objects.
- (viii) A director must act according to the company's Articles of Association.

(b) Liabilities of Directors Under Ca 2013

It is very important to note that, according to the Company Act, a person is selected as a director, although that he has responsibility not only for the offences of the Companies Act as well as he is also responsible for the various other statutes' offences, which includes Income-tax Act, GST, Labour legislation, the Shops and Establishment Act, 1947, the Negotiable Instruments Act, 1881 etc. The director's responsibilities are both collective as well as joint and for each action that is harmful to any company's interests. However, the Company and the Director both are considered as different objects, but as mentioned in below case on Company's behalf director is held liable:

- (i) Failure in making disclosures as stipulated SEBI (Prohibition of Insider Trading) Regulations, 1992 and SEBI (Acquisition of Shares & Takeovers) Regulations, 1997 by the directors may attract legal proceedings by SEBI
- (ii) Fraudulent Business Conduct and all associated debts and contracts executed
- (iii) Civil Liability in case of misstatement in Prospectus

- (iv) To pay for qualification shares
- (v) Excess in share application money or refunding of share application
- (vi) Tax Liability: Unless any Past Director or a Director is able to prove that tax's non-payment or non-recovery is attributable as breach of duty or gross negligence, at that time any past or present Director (related to the defaulter's time period) has the responsibilities to pay the associated penalty and tax amount shortfall.

Under CA 2013, supervisors can be considered responsible as organization "officers". "Officer" described to involve organization supervisors, among others. CA 2013 includes the idea of an "officer who is in default" comparable to any infringement by the organization of the arrangements of CA 2013 to put risk on that individual. The extent of 'the defaulting officer' is very wide and includes, in addition to other things: each full-time chief (3);

(c) Penal Provisions

For ensuring the appropriate adherence to Responsibilities and Duties laid out, there are several penal provisions in the Companies Act. The "Officer in Default" concept was Board of Directors' inclusive in Companies Act 1956. Further, in Companies Act 2013, under Section 2 (60), under duty lapse "Officer who is in Default" idea was specified in the situations that for any act provision the officer is in default as well as is considered to be these contraventions' part either participation or self with no objection is responsible for punishment or penalty that may include imprisonment. Also Nominee Directors can also be included by the Director under scrutiny. This is considered as a sensitive matter, as in cases where Director is not these meetings' part, however, had contravention information through any means is then responsible as well as partly accused for these acts. Therefore, this is significant that Director's voice of objection must be recorded mandatorily for avoiding these implications on innocent persons.

Under Companies Act 2013, there exists a high penalty amount in denomination as well as in comparison to the 1956 amendment these amounts are very stringent. INR 2,500/- is considered as the minimum applicable fine, however, it can be greater than INR25Crore. Also, as per Section 166 (codified duties), a fine between 1-5 lakhs is applied on Proven Defaulters. Few violations examples that can result in 1crore penalty as well as more are violations for provisions under:

- (i) Section 195 (2): Insider Trading
- (ii) Section 74 (3): Failure in deposits repayment within particular time
- (iii) Section 46: Share certificates' issuance and duplication with defraud intent
- (iv) Section 42: Securities subscription on Private Placement
- (v) Section 8 : Not for Profit companies,

As per Companies Act 2013, Section 149 (12), an Independent Director shall likewise be kept accountable for any actions due to or not faithfully performed by, the director in the proceedings of the Board of Directors, with his consent and knowledge. Therefore, this is significant with due caution that any Board proposal must be provided with a consent by Independent Directors. However, in these act of default cases, the law has observed the regardless of the Director's category summons are issued as well as for proving its innocence, it lies with the Director. Some defaulters are attracted imprisonment, majority non-cognizable under the Companies Act 2013. Although, offences associated with intent to fraud or committing fraud are cognizable (for arrest there is no need of warrant). Also, under section 66 offences associated with share capital reduction, under Section 56 shares' transmission or transfer with intent to defraud, under Section 36 for investment inducing fraudulently are cognizable, under Section 34 specifying misleading statements in the prospectus, and under Section 7 (6) furnishing false information or destroying any material information is cognizable.

Under Section 245, in Companies Act 2013, Shareholders or at least 100 Shareholders' group on all affected parties' behalf take "class action suit" for any wrong doing against the Directors as well as Company. For the shareholders, for expedited resolution National Company Law Tribunal took these. Additionally, to Companies Act 2013, various acts are interconnected as well as multiple conflicts dependent penal actions are attracted. Therefore, directors are required to have awareness of different laws' interdependencies as well as how their decisions can be influences that are still to be implemented.

(d) Nature of Contraventions under Ca 2013 – Non-Compoundable Vs. Compoundable

Non-Compoundable Offences: Although, there exists some serious infringements that are punishable with imprisonment and with fines (like fraud offences) or with imprisonment only, wherein company's officers that are defaulters or individuals involved with any company's establishment or its affairs' management become accountable as well as cannot be compounded/remedied only by putting penalties/fines. Such responsibilities are implemented on directors in case they are in default (involving non-executive directors) irrespective that they are company's directors or not.

Compoundable Offences: Under CA 2013, various infringements are of non-compliances' nature (including, giving loans to directors, deposits acceptance, provisions contravention regarding related party dealings, failure to file annual return etc. by the company) that entice either fines (in few cases punishable with imprisonment or fines or both). These offences are compounded or cured, subjected to Act's relevant provisions, through late payments of fines/penalties/fees as applicable.

(c) Liability under Few Other Laws

When a person is employed as a company's director, there exist some serious cascading effects regarding director's exposure to its responsibilities under several minor legislation. It has been observed from the some other legislations' brief study that for non-compliances, liabilities and duties thereof, through a company generally devolves with an individual in charge of company's management/business conducts.

Also, in some cases company's other officers/directors (whether non-executive or executive) held liable:

- (i) Wherein the commitment of offence is attributable to, or is with the connivance/consent of any neglect on such director's part; or
- (ii) These directors are employed by company (as per concerned authority's notification) to be company's management in charge as well as under some laws accountable for compliance (as owner/occupier) that permit for these nominations, failing which company's each directors.

Since under these laws, liabilities generally fall on individuals that are responsible to, and in charge of the company for conducting company's business, as a precaution, a specific person is designated by companies (as well as notifying the relevant government authorities) to be in charge for factory/relevant unit's compliances regarding some laws, (including under the Factories Act, 1948, appointing that person as manager or occupier for obedience).

IV SUGGESTED SAFEGUARDS AND PROTECTION

(a) Safeguards – Adopt a Precautionary Approach

In request for protecting their interests as well as dodge unnecessary obligation, this is prudent that director embrace a preparatory methodology. The following are a portion of the safeguards that can be thought of and upheld:

- (i) To go to meetings routinely;
- (ii) To be inquisitive and abuse plans for uncommon things and to look for further information in writing if vital;
- (iii) Guarantee that contradictions/dissenting opinions are recorded in the minutes;
- (iv) Acting genuinely as well as with appropriate defense;
- (v) Reporting worries about unscrupulous direct, actual or associated misrepresentation or infringement with the company's set of accepted rules or morals strategy;
- (vi) Set up review panels to look for professional exhortation and, if the circumstance demands, draw in outer offices;

- (vii) Involving outer offices to address issues with whistle blowing. For whistle blowing, the Company might consider employing an external reporting organization;
- (viii) Consider excusing yourself in instances of contention from participating in proceedings to give vital exposures of interests/clashes;
- (ix) Have a skilful ongoing and everyday consistence group and set up councils (for occasional internal reviews, and so on); and
- (x) Include pay arrangements in the appointment letter as well as look for Director and Officer Organization risk insurance ensure against noxious action (6).

(b) Some Recommendation

Lastly, as a general rule, it is always recommended to the directors:

- (i) For declaring an interest in a proposed arrangement or transaction.
- (ii) For exercising reasonable diligence, skill and care in exercising their powers
- (iii) For exercising independent judgment in all decisions.
- (iv) For promoting the company's success for its share holders' benefits
- (v) For acting within powers according to the company's incorporation documents as well as using powers for the authorized purposes.
- (vi) To avoid conflicts of interest.

Including these aspects, all directors are imposed with fiduciary duties as well as with a duty of care and skills by common law. Further, it is significant to observe that once director resigns, it does not result in ceasing the fiduciary duties of being a director. These duties include: the duty of confidentiality, the duty not to make an unauthorized profit and the duty to avoid conflicts of interest which sustained after the director's resignation.

(c) Limited Liability of Independent Director and Non-Executive Directors

To an organization, Independent Director considered as a mentor and guide. Their function involves enhancing credibility as well as corporate governance standards by working as an independent third party and help in handling risk. Such directors are responsible for ensuring proper governance by creatively and proactively involving in various committees set up by company. The independent directors are needed as they performs the following significant functions, including but not limited to

- (i) facilitate enduring as well as countering pressures from owners,
- (ii) in succession planning, fulfilling a helpful role
- (iii) on issues like standards of conduct, key appointments, resources, risk management, performance, and strategy he must support in acquiring independent judgment to bear on the board's discussions,

- (iv) whereas calculating the company's management and board performance that bring an objective view and
- (v) examining, supervising and describing performance of management regarding objectives and goals agreed in the board meetings.

In the companies, directors are designated according to Companies Act, 2013, section 149 and section 149 sub section 12 offers for the situations wherein Non-Executive Directors and Independent Directors' liabilities can be secured. Further, it has been significant to observe that, only when below situations are met, then only Non-Executive and Independent Directors are held liable, which are:

- with his connivance or consent or where he hadn't acted meticulously; and
- Acts of commission or omission through companies that took place with his awareness, attributable through Board Process. In case, such situations are not met then Non-Executive/Independent Directors cannot be held responsible under any circumstances.

V CONCLUSION

The above examination is giving broad guidelines for somebody to decide to turn into the role of a Director, however it is not that difficult to contribute well and play the role a Director efficiently, if they satisfy their obligation in the wellbeing of the shareholders. In order to avoid any serious circumstances against them or against the company, the directors must be more prepared now than before. They must attend various board meetings as well as must be completely conscious of the business of the companies. Before joining a board meeting, they need to arrive very prepared and alert. Interest in the meeting alone is not, at this point adequate, it is additionally important to guarantee that every communicated questions or inquiries are suitably recorded in the meeting minutes, which is significant and critical proof to maintain a strategic distance from legitimate issues sometime in the future. Proper training is needed for Directors who take up this role and the same will equip them to work in the organization's best interest. It must be guaranteed by itself that the directors do not remain unadvised, but in case of critical situations or doubts legal advice will be prudent practise for someone who is relatively less knowledgeable or inexperienced. Liability insurance for directors is now very important for directors. In the very heart of the business system, a significant part is played by the Companies Act 2013 in Corporate Governance enactment. Corrupt people can be holding the necessary shield due to fear for some time, although, the fact that these rules are being circumvented may not be long. Corporate governance needs to be imbibed by tangible benefits to the followers in the

soul of the system, if only then it resulted in companies' goal as well as is thoroughly pursued. One of the best thing is that companies' each shareholders and stakeholders believe in the Companies Act as well as this will help in continually clarify the pathway to universal corporate governance.

A significant part is played by the Companies Act 2013 in Corporate Governance enactment in the companies system's very core. Although, it relies on adherence for survival rather than adherence to purpose that like every earlier amendments might result in its failure. During assurance of the interest of the shareholders, it should be more straight forward. Corrupt people can be holding the necessary shield due to fear for some time, although, the fact that these rules are being circumvented may not be long. Corporate governance can only be imbedded into the system's soul by supplying the followers with tangible advantages, if only then it resulted in companies' goal as well as is religiously practised. One of the best things is that companies' each shareholders and stakeholders believe in the Companies Act as well as this will help in enlightening the universal Corporate Governance's path.

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