

**Roles,
Responsibilities &
Liabilities of
Directors in India**

July, 2011

INDEX

	Pages Nos.
INTRODUCTION	1
1. The Company and its Director	2
• Types of Companies	2
➤ Public Company vs. Private Company	2
➤ Holding and Subsidiary relationship	2
➤ Private Company being a subsidiary of a Public Company	3
• Director as a person within the Company	3
• Role played by a Director within the Company	3
• Director as an Authorized Representative of the Company	4
• Director as an ‘officer in default’	4
2. Classification of Directors	5
A. Classification under the Companies Act	5
➤ Categories of Directors	5
➤ Further classifications of Directors	5
B. Classification under the Listing Agreement	6
➤ Categories under the Listing Agreement	6
➤ Executive and non-executive Directors	6
➤ Independent Directors	7
3. Appointment of Directors – Process, Qualifications & Disqualifications	8
• Who can be appointed as a Director	8
• Appointment of Directors	8
• Appointment of Managing Directors	8
• Remuneration	8
• Qualifications of Directors	8
• Conditions for appointment as Managing / Whole-time Directors; Disqualifications	9
• Restriction on number of Directorships	10
• Director Identification Numbers	10
• Additional disqualifications in case of a public company	10

•	Additional disqualifications in case of a “pure” private company	10
•	Additional disqualifications for Managing and Whole-time Directors	10
•	Retirement of Directors	11
•	Removal of Directors	11
•	Vacation of office	11
•	Resignation	12
•	Compensation for loss of office	12
4.	Duties to be Discharged by Directors	13
A.	Fiduciary Duties	13
•	Good faith and bona fide acts	13
•	Proper use of powers	13
•	Unfettered Discretion	13
•	Lack of Conflicting Interests	13
B.	Common Law Duties	14
•	Duty to exercise reasonable skill and care	14
•	Duty to act within the powers of the company	14
•	Duty to exercise independent Judgment	14
•	Duty of Supervision	14
•	Duty of Confidentiality	15
C.	Specific Duties prescribed under the Companies Act	15
1.	Administration and Compliance	15
➤	Filing returns with the Registrar of Companies	15
➤	Convening Shareholders’ Meetings	15
➤	Approval of Company’s Documents	15
➤	Audit Requirements	15
2.	Restriction on Activities and Disclosure of Information	15
➤	Declaration of Interest	15
➤	Receipt of Compensation	15
➤	Attending Board Meetings	15
3.	Duties during Voluntary Winding Up of a Company	16
➤	Notice of resolution for Winding Up	16
➤	Declaration	16
➤	Notice of appointment of Liquidators	16

➤	Cease exercise of Powers	16
➤	Meeting of Creditors	16
➤	Filing Notice	16
4.	Duties during Involuntary Winding Up of a Company	17
D.	Additional Duties in case of a Listed Company	17
➤	Declaration of Pecuniary Relationships	17
➤	Declaration of Material Contracts	17
E.	Other Important Duties	17
➤	Duties under Foreign Exchange Management Act	17
➤	Duties under the Negotiable Instruments Act	18
➤	Duties under the Competition Act	18
➤	Duties under Labour Laws	18
5.	Liabilities of Directors; Persons who can bring Actions against the Directors	20
A.	Director's personal liability	20
•	Liability for Tax	20
•	Debts of the Company	20
•	Liabilities for company's Contracts	20
•	Refund of Share application money	20
•	Liability to pay for qualification shares	20
•	Mis-statement in the Prospectus	20
•	Fraudulent Conduct of Business	21
•	Unlimited Liability	21
B.	Criminal Liability	21
•	Dishonoured Cheques	21
•	Mis-statement in Prospectus	21
•	Offences under the Income Tax Act	21
•	Offences under Labour Laws	21
C.	Lifting of Corporate Veil	21
•	Lifting the veil under the Companies Act	21
•	Lifting of veil as recognized by courts	21
D.	Derivative Action Suits against Directors	22
•	What is a Derivative Action?	22
•	Ultra Vires	22

•	Fraud on Minority	23
•	Required Resolution	23
•	To safeguard Interests of the Company	23
•	Individual Membership Rights	23
•	Prevention of Oppression and Mis-management	23
E.	Other Actions against Directors	23
•	Company	23
•	Liquidators, Creditors and Contributories / Members, following Winding Up, Reconstruction, Compromise and Arrangement	24
•	SEBI	24
F.	Indemnifying Directors	24

INTRODUCTION

Since the emergence of various corporate scandals in India over the past few years, there has been much attention and debate on the role of company Directors. There has been a lot of focus on independent Directors (and also, on nominee Directors). In particular, with India emerging as a preferred investment destination, there has understandably been a need to clarify the responsibilities of nominee Directors. As covered in this Note, the principles to determine the liabilities of Directors are, in large measure, common to all Directors, varying in degree depending on their respective roles and involvement in the company's affairs. Company law has known directorial duties and liabilities for decades and the principles of such obligations have been distilled for many years. To illustrate, the Supreme Court of India, while considering who is said to be responsible for the conduct of a company's business, especially the role of non-executive Directors, had this to say in 1973 (in the case of *Official Liquidator, Supreme Bank Ltd. v. P. A. Tendolkar*, AIR 1973 SC 1104); words that are of no less relevance today:

“It is certainly a question of fact...whether a director...had acted reasonably as well as honestly and with due diligence....A director may be shown to be so placed and to have been so closely and so long associated personally with the management of the company that he will be deemed to be not merely cognizant of, but liable for, fraud in the conduct of the business of a company even though no specific act of dishonesty is proved against him personally. He cannot shut his eyes to what must be obvious to everyone who examines the affairs of the company even superficially.”

This Note seeks to highlight the key principles of Directors' duties and liabilities in simple, easy-to-understand language even for a non-legal audience. It places this discussion of Directorial roles, duties and liabilities in its proper context, namely, within the company organization and with reference to the appointment process (including, qualification and disqualification criteria and benchmarks). The Note also summarizes the principal statutory duties of Directors and indicates key liabilities in various circumstances. Lastly, the Note addresses what types of actions can be taken against errant Directors and oppressive majority shareholders.

Only when businesses appreciate the roles and responsibilities of Directors, and understand the basis on which liabilities can attach to Directors as a result of their acts or omission, can they be in a better position to critically evaluate and properly structure their investments in India, or appreciate legal advice on such matters arising in respect of their commercial arrangements in this country. We hope that this Note will prove to be a useful overview of, and guide to, the Indian legal position on this important subject.

Siddharth Raja & Harish Narasappa
July 2011

PLEASE NOTE THAT THE CONTENTS OF THIS GUIDE ARE NOT MEANT TO BE A SUBSTITUTE FOR OBTAINING LEGAL ADVICE. THE GUIDE IS ONLY AN INTRODUCTION AND WE URGE YOU TO CONSULT YOUR LAWYER FOR SPECIFIC ADVICE.

1 :: The Company and its Director

Types of Companies

A company in India can, pursuant to the Companies Act, 1956 (the “**Companies Act**”), legally organize itself as:

- a. a private company, or
- b. a public company.

Whether the company is private or public, it can be organized with limited liability (by shares or by guarantee) or with unlimited liability.

In case of a public company, it can choose either to list its shares on a recognized Indian stock exchange or to be an unlisted public company.

Public Company vs. Private Company

The primary distinguishing characteristics of a private company vis-à-vis a public company are as follows:

- a. A private company can be incorporated by a minimum of two (2) members, as against a minimum requirement of seven (7) members for a public company.
- b. The minimum paid-up capital for a private company is currently one hundred thousand rupees (Rs. 100,000/-), compared to five hundred thousand rupees (Rs. 500,000/-) for a public company.
- c. The Companies Act regulates a public company more than a private company. These include the requirement for a special resolution to issue shares to non-members, a separate certificate for commencement of business and certain provisions relating to statutory meetings and submission of statutory reports.
- d. The maximum number of members of a private company cannot exceed fifty (50), while there is no such restriction for a public company.
- e. A private company cannot raise money from the general public.
- f. In a private company, the Directors can refuse to register the transfer of shares at their absolute discretion. In a public company, shares are freely transferable.

Holding and Subsidiary relationship

Two companies are said to be in a holding-subsidiary relationship, in terms of the Companies Act, if:

- a. the composition of the board of Directors of company A is controlled by company B; or
- b. company B holds more than fifty percent (50%) of the nominal value of the company A.

Further, if company B is a subsidiary of another company, C (in terms of the above matrix), company A also becomes a subsidiary of company C.

Private Company being a subsidiary of a Public Company

If the holding company is a public company incorporated under Indian law and the subsidiary is incorporated and organized as a private company, then the

subsidiary will not be a “pure” private company but a “private company, which is a subsidiary of a public company”.

Further, under the Companies Act, if the holding company is an overseas body corporate, and would be regarded a public company if it were incorporated in India, then the private Indian company being its subsidiary will lose its status as a “pure” private company and will be subject to various other compliance requirements pursuant to the Companies Act, which are to be met by, as if it were, a “private company, which is a subsidiary of a public company”.

Interestingly, if the private Indian company is a one hundred percent (100%) subsidiary of the overseas body corporate then its status, under the Companies Act, is not changed to that of a subsidiary of a public company.

A “private company, which is a subsidiary of a public company” is required to comply with several provisions of the Companies Act not otherwise ordinarily applicable to “pure” private companies; in many respects, a “private company, which is a subsidiary of a public company” represents a halfway house, arising from its shareholding status, as distinct from being incorporated as a public company.

Director as a person within the Company

The Companies Act defines a Director as including any person occupying the position of a Director, by whatever name called. Thus, a person who has been validly appointed or elected to the Board of Directors of the company and on whose behalf the relevant form has been filed with the concerned authorities, is considered to occupy the position of a Director, irrespective of any title that may have been agreed to between the company and such person.

A Director is a person charged with the conduct and management of the company’s activities. The Directors (as a body, the “**Board of Directors**” or the “**Board**”), act as a team, under the authority of a meeting that is properly convened and is duly quorate, without improper exclusion of any of the Directors. The Board, then, as a team, conducts and regulates the affairs of the company. The Companies Act empowers the Board to do all such activities as the company is authorized to exercise, unless any law or the constitutional documents of the company requires the exercise of the power, or the doing of any act or thing, to be by the company in general meeting.

Role played by a Director within the Company

Generally, a Director plays a dual role, (i) as an agent of the company; and (ii) as a person with a fiduciary duty to the company, while discharging his duties. A Director rarely has powers to discharge his duties as an individual Director. It is the Board that has the power and authority to carry on the activities of the company and to meet the business objectives of the company as a team.

Acting individually, a Director has no power to act on behalf of the company in any matter, except to the extent to which any power or powers of the Board have been delegated to him by the Board, within the limits prescribed under the Companies Act or any other law. Contracts entered into by a Director are binding on the company only if they are within his actual authority or if the articles of association of the company, or the company’s bye-laws or internal rules of management (“**Articles**”), provide for the delegation of such power by a Board resolution, whether or not such power has actually been delegated. The exception

is a Managing Director, who has ostensible authority to enter into contracts on behalf of the company.

Director as Authorized Representative of the Company

All contracts entered into by the company, and other documents that need to be signed shall be so signed by a representative of the company duly authorized by the company or its Board. A Director of the company may be duly authorized by the Board to be its authorized signatory. In so doing, it is necessary to highlight that the Director is actually acting on behalf of the company and not personally. This may be done by signing under the seal of the company, and specifically mentioning along with the signature that the individual signing the document is the authorized signatory of the company. For certain transactions, appropriate resolutions may have to be passed by the Board and the shareholders. Directors do not automatically, by virtue only of their position, have the right to enter into contracts on behalf of the company. They need to be duly authorized in this regard by the shareholders or the Board.

Director as an 'officer in default'

Under the Companies Act, liability for any default is usually not attributed to all members of the Board. In most instances under the Companies Act, liability is attributed for non-compliance with the provisions of the Companies Act only to an '**officer in default**'. The term 'officer in default' can cover the Managing Director, the Whole-time Director, the Manager, the Secretary of the company, or any person in accordance with whose instructions the Board is accustomed to act (oftentimes called a '*Shadow*' Director) and any person charged by the Board with responsibility for any such compliance. Where a company does not have a Managing Director, a Whole-time Director or a Manager, any Director specified by the Board, or where no such Director has been specified, all the Directors may be deemed to be 'officers in default'.

In certain circumstances, the Companies Act imposes a liability on all Directors. For example, in case of winding up of a company, the Directors must ensure that the books of account of the company are completed and audited up to the date of winding up order and submitted to the concerned court at the cost of the company, failing which, such Directors shall be liable for punishment for a term of imprisonment not exceeding one (1) year and fine for an amount not exceeding one hundred thousand rupees (Rs. 100,000/-).

* * * *

2 :: Classification of Directors

A. Classification under the Companies Act

Categories of Directors

The Companies Act refers to the following two specific categories of Directors:

1. Managing Directors; and
2. Whole-time Directors.

A Managing Director is a Director who has substantial powers of management of the affairs of the company subject to the superintendence, control and direction of the Board in question. A Whole-time Director includes a Director who is in the whole-time employment of the company, devotes his whole-time of working hours to the company in question and has a significant personal interest in the company as his source of income.

Every public company and private company, which is a subsidiary of a public company, having a share capital of more than Five Crore rupees (Rs. 5,00,00,000/-) must have a Managing or Whole-time Director or a Manager.

Further classification of Directors

Based on the circumstances surrounding their appointment, the Companies Act recognizes the following further types of Directors:

1. *First Directors*: Subject to any regulations in the Articles of a company, the subscribers to the Memorandum of Association, or the company's charter or constitution ("**Memorandum**"), shall be deemed to be the Directors of the company, until such time when Directors are duly appointed in the annual general meeting ("**AGM**").
2. *Casual vacancies*: Where a Director appointed at the AGM vacates office before his or her term of office expires in the normal course, the resulting vacancy may, subject to the Articles, be filled by the Board. Such person so appointed shall hold office up to the time which the Director who vacated office would have held office if he or she had not so vacated such office.
3. *Additional Directors*: If the Articles specifically so provide or enable, the Board has the discretion, where it feels it necessary and expedient, to appoint Additional Directors who will hold office until the next AGM. However, the number of Directors and Additional Directors together shall not exceed the maximum strength fixed in the Articles for the Board.
4. *Alternate Director*: If so authorized by the Articles or by a resolution passed by the company in general meeting, the Board may appoint an Alternate Director to act for a Director ("**Original Director**"), who is absent for whatever reason for a minimum period of three months from the State in which the meetings of the Board are ordinarily held. Such Alternate Director will hold office until such period that the Original Director would have held his or her office. However, any provision for automatic re-appointment of retiring Directors applies to the Original Director and not to the Alternate Director.
5. *'Shadow' Director*: A person, who is not appointed to the Board, but on whose directions the Board is accustomed to act, is liable as a Director of

the company, unless he or she is giving advice in his or her professional capacity. Thus, such a 'shadow' Director may be treated as an 'officer in default' under the Companies Act.

6. *De facto Director*: Where a person who is not actually appointed as a Director, but acts as a Director and is held out by the company as such, such person is considered as a *de facto* Director. Unlike a 'shadow' Director, a *de facto* Director purports to act, and is seen to the outside world as acting, as a Director of the company. Such a *de facto* Director is liable as a Director under the Companies Act.
7. *Rotational Directors*: At least two-thirds of the Directors of a public company or of a private company subsidiary of a public company have to retire by rotation and the term "rotational Director" refers to such Directors who have to retire (and may, subject to the Articles, be eligible for re-appointment) at the end of his or her tenure.
8. *Nominee Directors*: They can be appointed by certain shareholders, third parties through contracts, lending public financial institutions or banks, or by the Central Government in case of oppression or mismanagement. The extent of a nominee Director's rights and the scope of supervision by the shareholders, is contained in the contract that enables such appointments, or (as appropriate) the relevant statutes applicable to such public financial institution or bank. However, nominee Directors must be particularly careful not to act only in the interests of their nominators, but must act in the best interests of the company and its shareholders as a whole. The fixing of liabilities on nominee Directors in India does not turn on the circumstances of their appointment or, indeed, who nominated them as Directors. Chapter 4 and Chapter 5 that follow set out certain duties and liabilities that apply to, or can be affixed on, Directors in general. Whether nominee Directors are required by law to discharge such duties or bear such liabilities will depend on the application of the legal provisions in question, the fiduciary duties involved and whether such nominee Director is to be regarded as being in control or in charge of the company and its activities. This determination ultimately turns on the specific facts and circumstances involved in each case.

B. Classification under the Listing Agreement

The Securities Contracts (Regulation) Act, 1956, read with the rules and regulations made thereunder, requires every company desirous of listing its shares on a recognized Indian stock exchange, to execute a listing agreement ("Agreement") with such Indian stock exchange. This Agreement is in a standard format (prescribed by the Securities Exchange Board of India ("SEBI")), as amended by SEBI from time to time. The Agreement provides for the following further categories of Directors:

Categories under Listing Agreement

1. Executive Director;
2. Non-executive Director; and
3. Independent Director.

Executive and non-executive Directors

An Executive Director can be either a Whole-time Director of the company (i.e., one who devotes his whole time of working hours to the company and has a

significant personal interest in the company as his source of income), or a Managing Director (i.e., one who is employed by the company as such and has substantial powers of management over the affairs of the company subject to the superintendence, direction and control of the Board). In contrast, a non-executive Director is a Director who is neither a Whole-time Director nor a Managing Director. Clause 49 of the Agreement prescribes that the Board shall have an optimum combination of executive and non-executive Directors, with not less than fifty percent (50%) of the Board comprising non-executive Directors. Where the Chairman of the Board is a non-executive Director, at least one-third of the Board should comprise independent Directors and in case he is an executive Director, at least half of the Board should comprise independent Directors. Where the non-executive Chairman is a promoter of the company or is related to any promoter or person occupying management positions at the Board level or at one level below the Board, at least one-half of the Board of the company shall consist of independent Directors.

Independent Directors

The Agreement defines an “**Independent Director**” as a non-executive Director of the company who:

- a. apart from receiving Director’s remuneration, does not have material pecuniary relationships or transactions with the company, its promoters, its Directors, its senior management, or its holding company, its subsidiaries, and associates which may affect independence of the Director;
- b. is not related to promoters or persons occupying management positions at the board level or at one level below the board;
- c. has not been an executive of the company in the immediately preceding three (3) financial years;
- d. is not a partner or an executive or was not a partner or an executive during the preceding three (3) years, of any of the following:
 - i. the statutory audit firm or the internal audit firm that is associated with the company, and
 - ii. the legal firms and consulting firms that have a material association with the company;
- e. is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect the independence of the Director; or
- f. he is not a substantial shareholder of the company, i.e., owning two percent (2%) or more of the block of voting shares; and
- g. he is not less than twenty-one (21) years of age.

Nominee directors appointed by an institution that has invested in, or lent money to, the company are also treated as independent Directors.

3 :: Appointment of Directors – Process, Qualifications & Disqualifications

Who can be appointed as a Director

Appointment of a Director is not only a crucial administrative requirement, but is also a procedural requirement that has to be fulfilled by every company. Under the Companies Act, only an individual can be appointed as a Director; a corporate, association, firm or other body with artificial legal personality cannot be appointed as a Director.

Appointment of Directors

Generally, in a public company or a private company subsidiary of a public company, two-thirds of the total numbers of Directors are appointed by the shareholders and the remaining one-third is appointed in accordance with the manner prescribed in Articles failing which, the remaining one-third of the Directors must be appointed by the shareholders. The Articles of a public company or a private company subsidiary of a public company may provide for the retirement of all the Directors at every AGM.

In a private company, which is not a subsidiary of a public company, the Articles can prescribe the manner of appointment of any or all the Directors. In case the Articles are silent, the Directors must be appointed by the shareholders.

The Companies Act also permits the Articles to provide for the appointment of two-thirds of the Directors according to the principle of proportional representation, if so adopted by the company in question.

Nominee Directors can be appointed by a third party or by the Central Government in case of oppression or mismanagement.

Appointment of Managing Directors

A Managing Director must be an individual and can be appointed for a maximum term of five (5) years at a time.

A person who is already a Managing Director / Manager of a public company or a private company subsidiary of a public company can become the Managing Director / Manager of only one other company (whether private or public) with the prior unanimous approval of the Board of such company. However, no such restrictions are applicable to a Manager or a Managing Director of “pure” private companies.

In case of a public company or a private company that is a subsidiary of a public company, if the appointment is not in accordance with Parts I and II of Schedule XIII of the Companies Act, such appointment must be approved by the Central Government.

Remuneration

In the case of a public company or a private company which is a subsidiary of a public company, the remuneration payable is subject to the provisions of the Companies Act, and may be determined either by the Articles or, if the Articles so provide, by a special resolution of the company in general meeting.

Qualifications of Directors

The Companies Act does not prescribe any qualifications for Directors of any company. An Indian company may, therefore, in its Articles, stipulate qualifications for Directors. The Companies Act does, however, limit the specified share

qualification of Directors which can be prescribed by a public company or a private company that is a subsidiary of a public company, to be five thousand rupees (Rs. 5,000/-).

*Conditions for appointment
as Managing / Whole-time
Directors; Disqualifications*

The Companies Act, under Schedule XIII, also prescribes certain other conditions that are to be fulfilled for the appointment of a Managing or a Whole-time Director or Manager in case of a public company and a private company that is a subsidiary of a public company. Accordingly, no person shall be eligible for appointment as a Manager, a Managing Director or a Whole-time Director if he or she fails to satisfy the following conditions:

1. He or she should not have been sentenced to imprisonment for any period, or a fine imposed under any of the following statutes, namely:
 - i. The Indian Stamp Act, 1899;
 - ii. The Central Excise Act, 1944;
 - iii. The Industries (Development and Regulation) Act, 1951;
 - iv. The Prevention of Food Adulteration Act, 1954;
 - v. The Essential Commodities Act, 1955;
 - vi. The Companies Act, 1956;
 - vii. The Securities Contracts (Regulation) Act, 1956;
 - viii. The Wealth Tax Act, 1957;
 - ix. The Income Tax Act, 1961;
 - x. The Customs Act 1962;
 - xi. The Monopolies and Restrictive Trade Practices Act, 1969 – now the Competition Act, 2002;
 - xii. The Foreign Exchange Regulation Act, 1973 – now the Foreign Exchange Management Act, 1999;
 - xiii. The Sick Industrial Companies (Special Provisions Act) 1985;
 - xiv. The Securities Exchange Board of India Act, 1992; and / or
 - xv. The Foreign Trade (Development and Regulation) Act, 1973.
2. He or she should not have been detained or convicted for any period under the Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974.
3. He or she should have completed twenty-five (25) years of age, but be less than the age of seventy (70) years. However, this age limit is not applicable if the appointment is approved by a special resolution passed by the company in general meeting or the approval of the Central Government is obtained.
4. He or she should be a managerial person in one or more companies and draws remuneration from one or more companies subject to the ceiling specified in Section III of Part II of Schedule XIII.

5. He or she should be a resident of India. ‘Resident’ includes a person who has been staying in India for a continuous period of not less than twelve (12) months immediately preceding the date of his or her appointment as a managerial person and who has come to stay in India for taking up employment in India or for carrying on business or vocation in India. However, this condition is not applicable for companies in the Special Economic Zone, as notified by Department of Commerce from time to time.

Restrictions on number of Directorships

The Companies Act prevents a Director from being a Director, at the same time, in more than fifteen (15) companies. For the purposes of establishing this maximum number of companies in which a person can be a Director, the following companies are excluded:

1. A “pure” private company;
2. An association not carrying on its business for profit, or one that prohibits the payment of any dividends; and
3. A company in which he or she is only appointed as an Alternate Director.

Failure of the Director to comply with these regulations will result in a fine of fifty thousand rupees (Rs. 50,000/-) for every company that he or she is a Director of, after the first fifteen (15) so determined.

Director Identification Numbers

All Directors of Indian companies are required to obtain Director Identification Numbers (“DINs”). Primarily, DINs are required to authenticate any electronic filings made by the company.

Additional disqualifications in case of a public company

In addition to the requirements mentioned above, the Companies Act further provides that a person shall not be eligible to be appointed as a Director of any other public company for a period of five (5) years from the date on which the public company, in which he or she is a Director, has failed to file annual accounts and annual returns or has failed to repay its deposits or interest thereon or redeem its debentures on the due date or pay dividends declared.

Additional disqualifications in case of a “pure” private company

A private company that is not a subsidiary of a public company can, by its Articles, provide that a person shall be disqualified for appointment as a Director on any grounds in addition to those specified in the Companies Act.

Additional disqualifications for Managing and Whole-time Directors

An individual cannot be appointed as a Managing or a Whole-time Director of a company if he or she:

1. is an undischarged insolvent, or has at any time been adjudged an insolvent;
2. suspends, or has at any time suspended, payment to his or her creditors, or makes, or has at any time made, a composition with them; or
3. is, or has at any time been, convicted by a court of an offence involving moral turpitude.

These requirements are not only more stringent than the requirements for an ordinary Director, but are also of an absolute and mandatory nature.

Retirement of Directors

In any public company or a private company that is a subsidiary of a public company, one-third of the Directors must retire at every AGM. However, every retiring Director is eligible for re-appointment. If the vacancy is not filled and the meeting has not expressly resolved to fill such vacancy, he or she shall be deemed to have been re-appointed until the next election meeting, unless he or she is not otherwise disqualified or is unwilling to so act as a Director or no resolution for such appointment has been put to the meeting and lost.

Removal of Directors

A Director can be removed by an ordinary resolution of the general meeting after a special notice has been given, before the expiry of his term of office. However, this is not applicable to Directors appointed by proportional representation or the Directors appointed by the Central Government.

Vacation of Office

The office of a Director of a public company, or of a private company which is a subsidiary of a public company, becomes vacant if he or she:

1. Becomes subject to any of the three (3) disqualifications mentioned above (with regard to disqualifications for a Managing or a Whole-time Director) during his or her term of office;
2. Fails to obtain within any time period as may be specified in the Articles (two months in case of a public company), or at any time thereafter ceases to hold, the necessary share qualification if any as prescribed by the Articles;
3. Absents himself or herself from three (3) consecutive meetings of the Board, or from all meetings of the Board for a continuous period of three (3) months, whichever is longer, without obtaining leave of absence from the Board;
4. Whether by himself or herself, or by any person on his or her account or any firm in which he or she is a partner or company in which he or she is a Director, accepts a loan or guarantee or security for a loan from the company in contravention of the requirements governing loans etc to Directors;
5. Acts in contravention of the requirements regarding disclosure of interests;
6. Is removed from office under the Companies Act; or
7. Having been appointed as Director by virtue of his or her holding an office or other employment in the company (for instance, that of Managing Director), he or she fails to hold such office or other employment.

Also, in such public companies and private companies that are subsidiaries of public companies, if a Director or his or her relative holds an office of profit without the consent of the company, and with such Director's knowledge, such Director shall be deemed to have vacated his or her office.

In addition to these reasons for the Director's office becoming vacant, a "pure" private company may prescribe other such reasons in its Articles.

If a person continues to act as a Director, despite knowing that his or her office has become vacant, he shall be punishable with a fine up to five thousand rupees (Rs. 5,000/-) for every day that he or she continues to function and act as such.

Resignation

The Companies Act is silent with respect to resignation of Directors. However, in a majority of cases, the Articles provide for Directors to resign. Even in cases where the Articles are silent, there is no absolute bar on Director's resigning, which becomes effective upon submission of such resignation letter and the filing of the necessary form for such resignation with the Registrar of Companies (whether or not the Board formally accepts the same, unless the Articles provide otherwise). The filing of such resignation related form with Registrar of Companies is an obligation to be discharged by the company in question.

The only exception to the above rule is in the case of Managing, Whole-time and Executive Directors who are employees of the company, and where the terms of their respective service contracts will ordinarily refer to resignations, notice periods and / or compensation in lieu thereof.

Compensation for loss of office

Only a Managing Director, a Director holding the office of a Manager and Whole-time Directors can receive compensation for loss of office or consideration for retirement, subject to the conditions specified by the Companies Act.

* * * *

4 :: Duties to be Discharged by Directors

Each Director has a fiduciary duty towards the company. All the powers entrusted to the Directors are only exercisable by them in this fiduciary capacity. The duties of Directors can be discussed under the following broad heads:

- A. Fiduciary duties;
- B. Common law duties;
- C. Specific duties prescribed under the Companies Act;
- D. Additional duties in case of a listed company; and
- E. Other statutory duties.

A. Fiduciary Duties

A Director owes fiduciary duties towards the company, and not to individual shareholders, creditors (other than during winding up when their interest has to be taken care of) or fellow Directors. These generally consist of the following:

Good faith and bona fide acts

Directors must act honestly, without negligence and in good faith in the *bona fide* best interests of the company. While applying this rule, Directors are not expected to act purely for the economic advantages of the company, disregarding the interests of the members, employees or creditors. The presumption is that a Director, acting within his or her authority, has acted in good faith, though the act may have been foolish or wrong, unless proved otherwise. The Courts usually refuse to substitute their judgment for the commercial judgment of the Director.

Proper use of powers

Directors must not exercise the powers conferred upon them for purposes different from those for which they were conferred. Notwithstanding that Directors have acted in honest belief for what they believe to be for the benefit of the company, they may nevertheless be liable for improper use of their powers, especially for purposes collateral to what they have been conferred for, for instance, furthering the Director's own interests or diluting the majority shareholding. A breach occurs when the dominant purpose of the act is improper.

Unfettered Discretion

Directors must not fetter their discretion for any reason whatsoever. They cannot validly contract or act pursuant to any arrangement either with one another or with third parties as to how they shall vote at board meetings or otherwise conduct themselves in the future. However, this does not include contracting to take further action to give effect to a contract entered into in a *bona fide* exercise of such discretion. Nominee Directors must be particularly careful not to act only in the interests of their nominators, but must act in the best interests of the company and of its shareholders as a whole.

Lack of Conflicting Interests

Directors must not, without the informed consent of the company, place themselves in a position in which their personal interests or duties to other persons are liable to conflict with their duties to the company or where there is a real and distinct possibility of conflict. This requirement covers the following aspects:

- i. Directors have to make continuous disclosures of their interests in the various transactions of, and with, the company. A Director cannot enter into a contract with the company without its informed consent, even if there is no unfair advantage to be gained, or abuse of position, by such Director.
- ii. Directors cannot use, without the consent of the company, the company's properties, opportunities or information for their own profit. In order to establish a breach of this duty, it must be shown: (1) that what the Directors did was so related to the affairs of the company that it can be said to have been done in the course of their management and in utilization of their opportunities and special knowledge as Directors, and (2) that what they did resulted in a profit to themselves. The English Courts, adopting a strict approach, have held directors to be in breach of this fiduciary duty, even if the opportunity was not one which would have been of use to the company. Indian courts generally follow this strict English law approach.
- iii. Directors have a duty not to compete with the company, which is in many respects a corollary of the immediately preceding rule.

B. Common Law Duties

A Director is required to discharge certain common law duties towards the company, which generally consist of the following:

Duty to exercise reasonable skill and care

This rule consists of two elements:

- i. an (objective) duty of care; and,
- ii. a (subjective) duty to exercise skill.

Imposition of a duty of care on the Director does not necessarily require that a Director must be a professional. A comparison with a particular Director in the same position and how such particular Director reasonably ought to have acted is the question to be asked. Therefore, the question of what functions should be carried out by a Director will depend on factors such as type and size of the company; the sector in which it operates; the Director's own personal skill and experience; the Director's position and role in the company; and the remuneration of the Director.

Duty to act within the powers of the company

Directors must act within the powers of the company. They must ensure that they are familiar with the company's Memorandum and Articles and being 'insiders', they must ensure they act in accordance with these provisions, since breaching any of them might lead to strict liability even in the case of an understandable mistake. Their powers under the company's Memorandum and Articles must be exercised for proper purposes in the interests of the company.

Duty to exercise independent Judgment

Directors should not take decisions at the direction of others. Even while taking the advice of others, as and when required, they should exercise independent judgment in considering recommendations and suggestions made by advisors.

Duty of Supervision

The Directors have a duty to exercise supervision over the officers of the company to whom they delegate powers.

Duty of Confidentiality The Directors have a duty of confidentiality towards the company and should not disclose or make use of confidential information relating to the company for any purposes, other than for the benefit of the company.

C. Specific Duties prescribed under the Companies Act

In addition to those already specified above, the Board, as against the individual Directors, is also required to discharge the following specific duties as prescribed under the Companies Act:

1. Administration and Compliance

Directors are vested with a number of administrative responsibilities in order to enable them to manage and administer the company. These administrative responsibilities include, amongst others, the following:

Filing returns with the Registrar of Companies Directors must file a return of allotment of shares within thirty (30) days with the Registrar, stating the number and nominal amount of shares comprising the allotment, the names, addresses and occupations of the allottees, and the amount, if any, paid or due and payable on each share.

Convening Shareholders' Meetings Directors must convene the different kinds of shareholders' meetings provided for in the Companies Act, within their stipulated periods.

For example:

- A statutory meeting should be convened after one (1) month but within six (6) months from the date on which a public company is entitled to commence its business;
- The first AGM should be convened within eighteen (18) months from the date of incorporation; and
- An extraordinary general meeting must be convened by the Directors on a requisition by members holding at least ten percent (10%) of the paid up capital of the company.

Approval of Company's Documents Directors must approve the balance sheet and profit and loss account of the company before it is signed on their behalf.

Audit Requirements In cases of winding up or liquidation, the Directors must ensure that the books of account of the company are completed and audited up to the date of winding up order issued by the Company Court.

2. Restriction on Activities and Disclosure of Information

The Companies Act has prescribed and / or supplemented the common law duties with certain other obligations on Directors that relate to their position, including the following:

Declaration of Interest Directors, who are concerned or interested in a proposed contract or arrangement with the company in any way, must disclose the nature of their concern or interest to the Board.

Receipt of Compensation Directors must not receive, in connection with a transfer of property or shares of the company, any payment as compensation for loss of profit or in

consideration for retirement from office. If they do so, they must hold such an amount in trust for the company.

Attending Board Meetings

Directors are under an obligation to attend the board meetings as prescribed by the Articles, or such as may be called by the chairman (if any) of the Board, otherwise any absenteeism for three (3) consecutive meetings or for a period of three (3) months, whichever is longer, without obtaining leave of absence, will result in that Director or Directors vacating their respective offices.

3. Duties during Voluntary Winding Up of a Company

The Directors must file the petition for winding up of the company (in a voluntary liquidation situation) before the relevant court. The Directors are also required to file a statement of the affairs prior to the voluntary winding up of the company, upon appointment of an official liquidator by the court. The following other duties are also required to be discharged, in connection with the winding up of the company:

Notice of resolution for Winding up

In the case of a voluntary winding up, the Directors must ensure publication of the notice of the resolution in the Official Gazette and a newspaper in circulation in the district where the registered office of the company is situated, within fourteen (14) days of the passing of such resolution.

Declaration

Where it is proposed to wind up a company voluntarily, the Directors of the company may at a meeting of the board, make a declaration verified by an affidavit, to the effect that they have made full inquiry into the affairs of the company, and as to the solvency of the company, i.e., the company has no debts, or that it will be able to pay its debts in full within such period not exceeding three (3) years from the commencement of the winding up as may be specified in the declaration.

Notice of appointment of Liquidators

Directors must give to the concerned Registrar of Companies a notice of the appointment of the liquidator of the company, so appointed by the company in the general meeting, and also give notice to such Registrar of Companies of the filling of any vacancy occurring in the office of such liquidator of the company.

Cease exercise of Powers

It is imperative for the Directors to cease exercising all powers of the Board, and likewise for the Managing or Whole-time Directors to cease exercise of such powers, except for the purpose of giving the notice of appointment of the liquidator mentioned in the immediately preceding paragraph.

Meeting of Creditors

In case of creditors' voluntary winding up, the Directors must cause a meeting of the creditors of the company to be called on the day or the next day on which general meeting is to be held and shall cause notices of the meeting to be sent to the creditors. At such creditors' meeting, the Directors must present a statement of the position of the company's affairs together with a list of creditors of the company and the estimated amount of such creditors' claims.

Filing Notice

The Directors must file the notice of any resolution passed at the creditors' meeting mentioned in the immediately preceding paragraph.

4. *Duties During Involuntary Winding Up of a Company*

In cases of involuntary winding up, the Directors must defend the Company in the winding up petition filed by a creditor or any other person recognized by the Companies Act. The requirement to file a statement of the affairs of the company by each of its directors, upon appointment of an official liquidator by the court, applies to involuntary winding up as well. In addition, the directors are also required to assist the official liquidator from time to time, by providing relevant information and assistance, in case of involuntary winding up of the company.

D. **Additional Duties in case of a Listed Company**

In case of a listed company, SEBI prescribes the following additional duties:

Declaration of Pecuniary Relationships

All pecuniary relationships and transactions of the non-executive Director vis-à-vis the company shall be disclosed in the annual report of the company. The non-executive Directors must disclose their shareholding (either held directly or for other persons on a beneficial basis) in the company in which they are proposed to be appointed as Director. Such disclosure shall be made prior to his appointment in a general meeting called for his appointment.

Declaration of Material Contracts

SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 require that the prospectus with respect to an initial public offering (IPO), or further public offer, shall disclose the dates, parties to, and general nature of the contacts appointing or fixing the remuneration of a Director within or more than two (2) years before the date of the prospectus. The company also needs to disclose the dates, parties to, general nature of every material contract not being in the ordinary course of business entered into more than two (2) years before the date of the prospectus.

E. **Other Important Duties**

Duties under Foreign Exchange Management Act

The Foreign Exchange Management Act, 1999, and the regulations issued thereunder, provide the legal framework for any transaction between an Indian entity and a foreign entity. It specifies that in case of contravention of any of its provisions or any rule, direction or order thereunder by a company, the person who at the time of the contravention was in charge of and was responsible to the company for the conduct of the business of the company shall be deemed to be guilty of the provisions and shall be liable to be proceeded against. If the offence is committed with the consent or connivance of, or is attributable to the neglect of the Director, such Director shall be deemed to be guilty and liable to be proceeded against.

For example: under the Foreign Exchange Management (Transfer or Issue of Securities by a Person Outside India) Regulations, 2000, a foreign entity can invest in an Indian company that undertakes activities in the construction-development of real estate sector, by way of Foreign Direct Investment, without requiring any approvals. However such investment by the foreign entity is subject to certain guidelines prescribed in that Regulation. Non-compliance of such conditions would be a contravention and any person being a Director of such company contravening those conditions can be found guilty.

Duties under the Negotiable Instruments Act

Under the Negotiable Instruments Act, 1881, if a company issues, and later dishonours a cheque which was presented for discharge of debt or other liability, every person who at the time of such dishonor was in charge of overall control of the day-to-day business of the company (both under law and as a matter of fact), shall be deemed to be guilty of the offence and shall be liable to be proceeded against.

If the offence is committed with the consent or connivance of, or is attributable to the neglect of the Director, such Director shall be deemed to be guilty and liable to be proceeded against. However, if such person has been appointed as a Director by virtue of his holding in any office or employment in the central government or state government or a financial corporation owned or controlled by the state or the central government, he shall not be liable for prosecution.

Duties under the Competition Act

The Competition Act, 2002 prescribes certain specific duties to be discharged by Directors.

1. *Combination:* The Competition Act, 2002, imposes certain limits to be examined, and adhered to, by Directors and requires that the merger or amalgamation or acquisition does not amount to a resultant enterprise being a combination.
2. *Duty to file report with Commission:* Directors must show that such a combination under the Competition Act, 2002, is not likely to cause an appreciable adverse effect on competition within the relevant market in India, if the assets or the turnover of the newly created or remaining company amounts to a combination by exceeding the prescribed limits. Therefore, it is the duty of the Director under this legislation, to give notice to the Competition Commission, in the form as may be specified and the fee which may be determined, by regulations, disclosing the details of the proposed combination, within seven (7) days of the company's approval of the merger or amalgamation proposal. The Commission shall then conduct such investigations, inquiries and pass any orders. No combination shall come into effect until two hundred and ten (210) days have passed from the day on which the notice has been given to the Commission or the Commission has passed orders, whichever is earlier.

Duties under Labour Laws

In legislations such as the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 and the Payment of Gratuity Act, 1972, the term 'employer' with respect to any establishment (in cases other than a factory), means the person who, or the authority which, has the ultimate control over the affairs of the establishment. Where the said affairs are entrusted to a Manager or a Managing Director, such Manager or Managing Director is considered the 'employer'.

However, this liability is not one imposed on all Directors or Managers uniformly; it is only imposed on those Directors or Managers who are in overall control of the affairs of the company (this implies control over the day-to-day affairs of the company). Those Directors who are only in control of certain aspects, or are aware of the policy of the company, but are not in charge of it, would not be held liable.

The Managing Director or the Manager, will, in his capacity as the 'employer', have the duty to ensure welfare of the employees. He will also be responsible to make necessary statutory registrations or contributions, as applicable, from time to time.

* * * *

5 :: Liabilities of Directors; Persons who can bring Actions against the Directors

Directors can be held liable both jointly and collectively, for any and every act, commission or omission which is prejudicial to the interests of the company and violates any of the duties to be discharged by them.

A. Director's personal liability

As a general rule, since the company and its Director are separate entities, the Director has no personal liability on behalf of the company. However, under certain circumstances, a Director may be held liable on behalf of the company. These circumstances are:

Liability for Tax

Under the Income Tax Act, 1961, where any tax due from a private company in respect of any income of any previous year cannot be recovered from such private company, then, every person who was a Director of such private company at any time during the relevant previous year is liable, jointly and severally, for the payment of such tax. A Director (including any past Director but only for the duration when he was in office) can, however, escape such liability if he or she proves that the non-recovery of such tax cannot be attributed to any gross neglect, misfeasance or breach of duty on his or her part in relation to the affairs of such private company.

Under the Central Sales Tax Act and certain state Sales Tax laws, liability may be fastened on Directors of a company, which is wound up, for recovery of sales taxes due from such liquidated company.

Debts of the Company

Generally, a Director is not personally liable for any debt of the company unless fraud on the part of such Director can be established.

Liability for company's Contracts

A Director is, generally, not liable for any contract entered into by the company, unless expressly provided for, or fraud on the part of such Director can be established.

Refund of Share application money

A Director is personally liable along with the company to repay the share application or excess share application money, as the case may be, if the same is not repaid within the stipulated time limit.

Liability to pay for qualification shares

If the Director has not acquired his or her qualification shares within the prescribed time period and the company goes into liquidation the day after this period expires, the Director will be called upon by the Official liquidator to pay for the shares he or she was supposed to have purchased.

Mis-statement in the Prospectus

Civil liability can be imposed on a Director for any untrue statement in the prospectus of a public company if he or she is a Director at the time of the issue of the prospectus, unless he or she proves that he or she withdrew consent before the issue of the prospectus or that it was issued without his or her authority or consent or without his or her knowledge or that, once he or she came to know of the untrue statement, he or she withdrew consent and gave reasonable public notice of the same, or proves that he or she believed the impugned statements to be true.

Fraudulent Conduct of Business A Director may be held personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company if he or she was knowingly party to the fraudulent carrying on of business.

Unlimited Liability The liability of any or all of the Directors of a limited company can be unlimited if so provided by the Memorandum, or can be so done if approved by a special resolution as authorized by the Articles.

B. Criminal Liability

Dishonoured Cheques The Director signing a cheque which is dishonoured so as to constitute an offence under the Negotiable Instruments Act, 1881, can be prosecuted along with the company.

Mis-statement in the Prospectus The Companies Act imposes criminal liability on any person who was responsible for a mis-statement in the prospectus of a public company.

Offences under the Income Tax Act An offence committed by a company under the Income Tax Act, 1961 is attributed to the persons who were responsible for and in charge of the business of such company.

Offences under Labour Laws An offence committed by a company under the various labour legislations (specifically in case of Employees Provident Funds and Miscellaneous Provisions Act, 1952 and Factories Act, 1948) is attributed to the persons who were responsible for and had control over the affairs of the company. Hence, Directors would be personally liable for offences committed by a company under the relevant labour legislations. However, this liability is not one imposed on all Directors uniformly; it is only imposed on such Directors who are in overall control of the affairs of the company (this implies control over the day-to-day affairs of the company). Those Directors who are not in overall charge of the company, but are only in control of certain aspects; or are aware of the policy of the company, but are not in charge of it, would not be held liable.

C. Lifting of Corporate Veil

A company is an independent entity and, as a general rule, the Director of the company is not liable for any offence or, breach or liability of the company. However, in certain cases, the common law doctrine of 'lifting the corporate veil' is utilized to impose penalty on the person, or persons, controlling in reality the actions of the company (such as, Directors) and certain statutes impose liability on such person or persons in charge of, or responsible to, the company for the conduct of its business.

Lifting the veil under the Companies Act If, in the course of winding up, it appears that any business of the company has been carried on with an intent to defraud the creditors of the company or any other person, or for any fraudulent purpose, the persons who were knowingly parties to the carrying on of the business in such fraudulent manner shall be personally responsible without any limitation of liability, for all or any of the debts or other liabilities of the company as the court may direct.

Lifting of Veil as recognized by courts The scope of this principle as applied by Indian courts is broad and largely dependent on the facts of an individual case. The corporate veil may be lifted where:

1. a statute itself contemplates this;
2. where fraud or improper conduct is intended to be prevented;
3. where a taxing statute or a beneficial statute is sought to be evaded; or
4. where associated companies are inextricably connected as to be, in reality, part of one concern.

The nature of the impugned conduct, the involvement of the public interest and the effect on the affected parties are all relevant considerations while determining whether or not to lift the corporate veil.

The court has, in one instance, lifted the corporate veil and recognized an individual as having acted on behalf of the company, who had resigned from the Board of a company and had ceased to be member of the company.

D. Derivative Action Suits against Directors

Courts will not, generally, interfere at the instance of the shareholders with the management of a company by its Directors, so long as they are acting within the powers conferred on them by the Articles, except in cases of derivative actions as explained below.

What is a Derivative Action?

Derivative action is defined as an action by one or more shareholders of a company where the cause of action is vested in the company and relief is accordingly sought on its behalf. Since the company has a distinct legal personality with its own rights and liabilities which are different from those personal rights of individual shareholders, this action is brought by a shareholder not to enforce his or her own personal rights but, rather, the rights and liabilities of the company on its behalf and for the benefit of the company; which the company cannot itself do, as it is controlled by the 'wrong-doers'.

In order to be classified as a derivative action, the following aspects must be satisfied:

- It must be brought in a representative form, even though it is the company, rather than the other shareholders, whom the person initiating the legal action / proceedings seeks to represent. Thus, by implication, all the other shareholders are bound by the result of the action.
- Although the action is brought on behalf of the company, the company appears as a defendant, so that the action takes the form of a representative action by the initiating shareholder on behalf of himself and all the other shareholders (other than the alleged 'wrong-doers'), against the alleged 'wrong-doers' (who are, in fact, in control of the company) and the company. Derivative claims may be brought by a shareholder or shareholders in the following instances, as described below.

Ultra Vires

A shareholder may bring an action against the company and its Directors in respect of matters which are *ultra vires* the Memorandum or the Articles of the company and which no majority shareholders can sanction. For example, Directors of the company sanctioning an action that is contrary to the objects of the company.

<i>Fraud on Minority</i>	Directors and the company would also be liable if the conduct of the majority of the shareholders constitutes a “fraud on minority”, i.e., a discriminatory action. For example, where the shareholders have passed a special resolution with an effect of discriminating between the majority shareholders and minority shareholders, so as to give the former an advantage of which the latter were deprived.
<i>Required Resolution</i>	Certain actions of the company can be approved only by passing a special resolution at a general meeting of shareholders. If the majority seek to circumvent this legal requirement and pass only an ordinary resolution, or do not pass such a special resolution in the manner required by law, any member or members can bring an action to restrain the majority.
<i>To safeguard Interests of the Company</i>	For instance, an obvious wrong may have been done to the company by the Directors, but because of the control of such Directors on the majority shareholders, such shareholders may not permit an action to be brought against the ‘wrong-doer’ Directors. Therefore, to safeguard the interests of the company, any member or members may bring a derivative action.
<i>Individual Membership Rights</i>	As a general rule, personal rights <i>per se</i> are not to be enforced through derivative actions; however, some exceptions have been recognized. These exceptions often arise in cases of rights that have been conferred upon the shareholders by the Companies Act itself or the respective Articles (commonly known as “individual membership rights”). For example, the right to vote, the right to have one’s vote recorded, or the right to be nominated as a candidate for the post of a Director during the election of Directors at a general meeting of the shareholders.
<i>Prevention of Oppression and Mis-management</i>	A representative action may be brought for prevention of oppression and mismanagement, which are cases where the majority acts in a manner that oppresses the minority; or where the affairs of the company are being conducted in a manner prejudicial to public interests or oppressive to any member(s) or in a manner prejudicial to the interests of the company including an adverse material change in the management or control of the company. Since these proceedings are initiated for the benefit of the company, it can be considered a form of derivative action and find specific place in the scheme of the Indian company law under the Companies Act. In order to obtain relief, the Company Law Board can be approached by: <ol style="list-style-type: none"> 1. Not less than one hundred (100) shareholders, or not less than one-tenth of the total number of members; or 2. Members holding not less than one-tenth of the issued shares capital of the company, provided all the dues on the shares have been paid by the applicants.

E. Other Actions against Directors

Actions can be brought against a Director for failure to discharge his or her duties. The following persons shall have the *locus standi* to bring such actions or proceedings against the Directors:

<i>Company</i>	As a general rule, Directors owe their duties to the company alone and would not generally owe their duties to the company’s shareholders, subsidiaries or holding companies (or, indeed, even the company’s creditors). In practice, such claims would, unless a company is insolvent, most likely arise as a result of a takeover or
----------------	--

after the make-up of the board has significantly changed for some other reason. There is also a possibility of claims being brought by the company against other third parties, in particular, auditors, who may be joined with Directors in proceedings, considering their contribution to the Directors' breach (if at all) of their duties to the company.

Liquidators, Creditors and Contributories / Members, following Winding up, Reconstruction, Compromise and Arrangement

The claims may arise because all has not been well with the company and that certain decisions were taken by Director / Directors who need to be held accountable for that decision. Normally, such claims relate to the fraudulent conduct of business when a company is in the course of winding up. These claims will arise when the company continues to carry on business and incur debts at a time when there is, to the knowledge of the Directors, no reasonable prospect of the creditors ever receiving payment of those debts. The Directors are personally liable in such a case for such debts of the company.

Claims may arise against Directors to furnish such information particularly stating material interests of the Directors or Managing Director of the company, whether in their capacity as such or as members or creditors of the company or otherwise. This is instrumental in gauging the effect of those interests on the compromise or arrangements so proposed. The Directors also owe a duty to the Official liquidator, where a winding up order has been made by the High Court, to submit and verify a statement as to the affairs of the company.

In all the aforementioned cases it is unlikely that such claims will be brought by the creditors or members and are in practice brought by a Official liquidator (duly appointed by the members or creditors or High Court) in the name of the company.

SEBI

In the case of listed companies, SEBI may proceed against the Director(s) where the Directors of a listed public company fail to make certain disclosures as stipulated under the SEBI (Acquisition of Shares & Takeovers) Regulations, 1997 and SEBI (Prohibition of Insider Trading) Regulations, 1992, in respect of their shareholdings in the company.

F. Indemnifying Directors

Indemnification

The Companies Act restricts the ability of a company to indemnify its Directors and officers against losses. Any provision contained in the Articles or any other agreement, to provide indemnity on account of their negligence, default, misfeasance and breach of duty or trust is void. However, such indemnity will be enforceable if it is against any liability incurred by such Director or officer in defending any proceedings in which judgment is given in his favour or in which he is acquitted or discharged or where it is determined that, although liable, he acted honestly and reasonably and should be excused. The Companies Act, however, does not prevent a company from taking an insurance policy for its own protection against loss caused to it by its Directors. Further, the Director can take out a policy to recompensate the loss he suffers because of his liability to the company. The premium for such policy may be paid by the company itself.

* * * * *

PARTNERS



HARISH B. NARASAPPA

harish@narasappa.com



ROOPA P. DORASWAMY

roopa@narasappa.com



SIDDHARTH RAJA

siddharth@narasappa.com



POORNIMA HATTI

poornima@narasappa.com

Narasappa, Doraswamy & Raja

Advocates & Solicitors

62/1 Palace Road • Vasanthnagar • Bangalore 560 052 • India.
Tel.: +91 80 4268 6000

© Narasappa, Doraswamy & Raja, 2011