CHAPTER- IV

ROLE OF DIRECTORS IN CORPORATE GOVERNANCE

The new Companies Act, 2013 makes a laudable contribution towards stipulation and elucidation of the duties and responsibilities of the directors of a company, more so of public limited companies. New Act not only fine tunes corporate governance but goes a long a way in growth and prosperity of corporate world in India; thereby removes the deficiencies of old Companies Act of 1956. The new Companies Act, 2013 can be seen as offering a landmark piece of legislation in this regard, which duly and explicitly clarifies, redefines, and enlarges the ambit of duties and responsibilities of the directors. These newly introduced provisions by Companies Act, 2013 regarding the duties and responsibilities of the directors, including the independent directors, not only provide greater certainty to the directors regarding their conducts and responsibilities, and thus, ensuring better and impeccable corporate management and governance; but also enable and empower the beneficiaries, regulators, and the courts, to judge, regulate, and control the activities and obligations of the directors more objectively and effectively. Ours this well-drafted web-article offers very useful and fertile information exclusively about these new provisions of the Indian Companies Act of 2013, connected with the roles, duties, and responsibilities of the directors and independent directors of public limited companies.

For duties and liabilities of the directors the legislation of Companies Act, 2013 is both fortified and enhanced by the revised corporate governance norms (Revised and New Clause 49 of the Listing Agreement) of SEBI [the Securities and Exchange Board of India], in order to bring the SEBI's corporate governance norms in connection with the listed companies, in close harmony and consistency with the provisions of the Companies Act, 2013.

While the several provisions of the Companies Act, 2013 related with duties of directors have been made effective from April 01, 2014; the revised SEBI's norms for corporate governance are likely to be in force from October 01, 2014.

121
Here, it may also be briefly just mentioned that the Directors are regarded as being the Key Managerial Persons of a company, with special importance to the listed companies. They can hold multiple high and responsible positions in the companies, such as the Managing Director, Manager, Whole Time Director, or an Independent Director. Thus, efficient, flawless, and rather progressive management of a company, and the desired growth and profitability of its businesses, are certainly largely dependent on the competence and trustworthiness of its directors. By the way, a Director means a Director appointed to the Board of a company; and, the Board of a company represents the collective body of its directors.

4.1 Legal Position of Director

I. **Directors as Agents**: A company as an artificial person acts through directors who are elected representatives of the shareholders and who execute decision making for the benefit of shareholders.

II. **Directors as employees**: When the director is appointed as whole time employee of the company then that particular directors shall be considered as employee director or whole time director.

III. **Directors as officers**: Director treated as officers of a company. They are liable to certain penalties if the provisions of the companies act are not strictly complied with.

IV. **Director as trustees**: Director is treated as trustees of the company, money and property: and of the powers entrusted to and vested in them only as trustee.

V. **Director as “Officer”** “officer” includes any director, manager or key managerial personnel or any person in accordance with whose directions or instructions the Board of Directors or any one or more of the directors is or are accustomed to act.

4.2 Appointment of Directors

The success of a company depends upon the integrity and competence of its directors. In *Indian States Bank Ltd. v. Sardar Singh*,¹ it was held that it is necessary that management of companies should be in proper hands. The

¹ AIR 1934 ALL 855.
appointment of directors is accordingly strictly regulated by the Act. There are now special provisions for preventing management by undesirable persons. One evil that is abolished by the Companies Act, 2013 is that of a company or firm acting as a director of another company. Now only an individual can be appointed as a director of a company and no company, firm or association can be appointed as a director.² No company is to appoint or appoint any individual as director unless he has been allotted a Director Identification Number under section 154.³

4.2.1 Board of Directors

Every company should have a board of directors⁴ consisting of individuals as directors. A public company is to have a minimum of 3 directors and a private company is to have 2 directors. In the case of one person company, only one director is compulsory. There can be a maximum of 15 directors. A company may appoint more than 15 only after passing special resolution. The Central Government may prescribe a class or classes of companies who are to have at least one woman director. These requirements are to be complied within 1 year of enforcement of the Act of 2013. Every company is to have at least one director who has stayed in India in the previous year at least for 182 days.⁵

4.2.2 Number of Directorships

A person cannot hold office of a director in more than 20 companies including alternate directorships at the same time. Where a director already holding office in 20 companies is appointed, the appointment shall not take effect and shall become void unless within 15 days he vacates his office in some companies to bring the number of directorships to 20. In the case of public company, the maximum number of public companies in which a person can be a director has been restricted to 10. The members of a company may by special resolution specify any number of companies in which a director of the company may act as directors. After the commencement of the Act, directors holding office in companies more than those permitted under the section have to choose the

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² Section 149 of Companies Act, 2013.
³ Section 152(3) of Companies Act, 2013.
⁴ Section 2(10) defines Board of Directors as “Board of Directors” or “Board”, in relation to a company, means the collective body of the directors of the company.”
⁵ Section 149 of Companies Act, 2013.
companies in which he would like to continue and intimate his resignation to others. After such resignation, he cannot accept directorship in more than the specified number except up to 1 year. Contraventions of the provision are punishable.⁶

4.2.3 Independent Directors

The liability regime of the Companies Act, 2013 not only imposes the above-mentioned duties and responsibilities on the directors of Indian companies, but also advocates for independence and equitableness of the board of a company, especially a public limited company. Consequently, the roles, duties, and responsibilities of the Independent Directors have also been stipulated by the new Indian Companies Act of 2013. An Independent Director is that member of the board of a company, who does not possess any financial relationship with the company (except the sitting fees), nor can own shares in the company. The earlier Indian Companies Act of 1956 had no explicit provisions for the independent directors, and only the Old Clause 49 of the Listing Agreement of SEBI contained prescriptions for induction of independent directors to the listed companies.

The new Indian Companies Act of 2013 dictates that every listed company must contain at least one-third of the total magnitude of its directors, as the independent directors; and it also empowers the Government of India to include other categories of companies within the scope of this provision or requirement⁷. Public limited companies composited as per the former Companies Act, 1956, are granted a transition period of one year for making strict compliance with this mandatory provision. Again, the independent directors are not permitted to hold office for more than two consecutive terms of five-year periods.

In the new regime, the roles and duties of the independent directors attained significant expansion, and many new other areas have been prudently covered. Broadly, they are intelligently assigned the highly responsible role of the arbiters among various constituencies within the corporation. Hence, the new provisions for the independent directors of the limited companies are certainly very constructive for transparent and sound corporate governance, and are hugely

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⁶ Section 165 of Companies Act, 2013.
⁷ Section 149 of the Companies Act, 2013.
beneficial to the company and its all shareholders. Some of the most significant functions, duties, and liabilities of the independent directors, are the following (According to the Schedule IV of the Companies Act, 2013):

I. To assist in forwarding equitable and independent judgment to the board
II. To secure and promote the interests of all stakeholders of the concerned company, particularly of the minority shareholders
III. To conciliate and balance the conflicting interests of the stakeholders
IV. To attend actively and constructively most of the board and committee meetings
V. To pay proper and adequate attention to Related Party Transactions (RPTs)
VI. To report concerns honestly and impartially about any unethical behavior, violation of the code of conduct, or any suspected fraud in the company

4.2.3.1 Manner of Election of Independent Directors and Maintenance of Data

Independent directors have to be selected from a data bank containing names, addresses and qualifications of persons eligible and willing to act as directors. This has to be maintained by any body, institute or association as may be notified by Central Government. A body to be notified should have expertise in creation and maintenance of such data bank and put it on their website for use by the company making the appointment of such directors. The responsibility of exercising due diligence before picking up a person from such data bank is to be that of the company. The appointment has to be approved by the company in general meeting. Data bank has to be maintained in accordance with the rules as may be prescribed. The Central Government may prescribe the manner and procedure of selection of independent directors who fulfil the qualification and requirements under the act.

4.2.4 Appointment of Directors elected by Small Shareholders

A listed company may have one director elected by such small shareholders as may be prescribed. For the purpose of this section a small

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8 Section 150 of Companies Act, 2013.
9 Section 150 (1) of Companies Act, 2013.
10 Qualification and requirements stated in section 149 of Companies act, 2013.
11 Section 151 of Companies Act, 2013.
shareholder is a shareholder holding shares of nominal value of not more than Rs.20,000 or such other sum as may be prescribed.

4.2.5 Appointment of First Directors

The first directors of the company are to be appointed by the subscribers of the memorandum which are listed in the articles of the company. If no appointment is made then all the subscribers who are individuals become directors. The first directors hold office only up to the date of first annual general meeting of the company and subsequent directors must be appointed in accordance with the provisions of the act.

In Usha chopra v. Chopra Hospital (P) Ltd. it was held that the appointment of directors in a two-member, two-director company both of them NRIs with no record of board meeting or notice to directors, was wrong and oppressive.

4.2.6 Appointment of Directors at General Meeting

The shareholders exercise control through their power of appointment of directors. The person to be appointed has to furnish his Director’s Identification Number and a declaration that he is not disqualified to become a director under the provision of the Companies Act. The person appointed as director has to file his consent to act as director. The consent is to be filed with the Registrar within 30 days of his appointment in the prescribed manner.

4.2.7 Appointment of Rotational Directors

The Articles of the company may provide for retirement of all the directors by annual rotation. Otherwise only 1/3 can be given permanent appointment. The effect of these provisions is that the rotational director has to be appointed at general meetings except where the act provides otherwise. This provision eradicates the mischief caused by self-perpetuating managements. In BR Kundra

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12 Section 152 of Companies Act, 2013.
14 According to section 2 (27) of Companies Act, 2013, “control” shall include the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner;
15 Section 152 (4) of Companies Act, 2013.
16 Section 152 (5) of Companies Act, 2013.
v. Motion Pictures Assn\textsuperscript{17} it has been held by the Delhi High Court that directors cannot prolong their tenure by not holding a meeting in time. They would automatically retire from office on the expiry of the maximum permissible period within which a meeting ought to have been held.

In Swapan Dasgupta v. Navin Chand Suchanti\textsuperscript{18} it was held that where a director to be rotated out is also holding the office of managing director, the latter office will also vacate with the former, but expiry of the term of, or removal from managing directorship, does not entail the cessation of his office as a director.

4.2.8 Reappointment of Directors at General Meeting

The vacancies thus created should be filled up at the same meeting but the general meeting may resolve not to fill the vacancies. If it has done neither, the meeting shall be deemed to have been adjourned for a week. If at the reassembled meeting also no fresh appointment is made, nor there is a resolution against appointment, the retiring directors shall be deemed to have been reappointed, except in the following cases.

(i) at that meeting or at the previous meeting a resolution for the reappointment of such director has been put to the meeting and lost;

(ii) the retiring director has, by a notice in writing addressed to the company or its Board of directors, expressed his unwillingness to be so re-appointed;

(iii) he is not qualified or is disqualified for appointment;

(iv) a resolution, whether special or ordinary, is required for his appointment or re-appointment by virtue of any provisions of this Act; or

(v) a motion to appoint two or more persons as directors by a single resolution, if passed without unanimous consent, being void under section 162, it shall not have the effect of reappointing rotated out directors.

\textsuperscript{17} (1976) 46 Comp Cas 339 (Del).
\textsuperscript{18} (1988) 64 Comp Cas 562; (1988) 3 Comp LJ 76 (Cal).
4.2.9 Fresh Appoint of Director at the General Meeting\textsuperscript{19}

If a new director is to be appointed in place of a retiring director, a notice in writing for his appointment should be left at the office of the company at least 14 days before the date of the meeting along with a deposit of Rs. 1,00,000 which shall be refunded if the candidate gets selected as a director or gets more than 25\% of total valid votes cast either on show of hands or on poll on such resolution. The company is required to inform the members about the candidature in prescribed manner.

In S Pazhamalai v. Aruna Sugars Ltd.\textsuperscript{20} it was held that it is not necessary for proposing a candidate by a special notice that the requirements of section 111 relating to circulation of member’s resolution be complied with.

In Namita Gupta v. Cachar Native Joint Stock Co Ltd.\textsuperscript{21} it was held that non-compliance with the requirements of procedure renders the appointment void. In this case the members were not informed.

In Prakash Roadlines Ltd. v. Vijaykumar Narang\textsuperscript{22} it was held that on receiving a notice the company becomes bound to inform the members and has no discretion in the matter.

4.2.10 Appointment of Director by Nomination\textsuperscript{23}

An agreement among the shareholders may be imbibed in the articles to the effect that every holder of 10\% shares shall have the right to nominate a director on the board. The phenomenon of nominee directors is now part of the corporate scenario. Subject to the articles of a company, the Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law for the time being in force or of any agreement or by the Central Government or the State Government by virtue of its shareholding in a Government company.

\textsuperscript{19} Section 160 of Companies Act, 2013.
\textsuperscript{20} (1984) 55 Comp Cas 500 (Mad).
\textsuperscript{21} (1999) 98 Comp Cas 655 (CLB).
\textsuperscript{23} Section 161 (3) of Companies Act, 2013.
4.2.11 Appointment by Voting on Individual Basis

At a general meeting of a company, a motion for the appointment of two or more persons as directors of the company by a single resolution shall not be moved unless a proposal to move such a motion has first been agreed to at the meeting without any vote being cast against it. A motion for approving a person for appointment, or for nominating a person for appointment as a director, shall be treated as a motion for his appointment. A person who has been appointed as a director for the first time is required to submit within 30 days of his appointment a written consent to act as a director to the Registrar of companies.

4.2.12 Appointment by Proportional Representation

It is apparent from that the basic method adopted for the appointment of directors is election by simple majority. All the directors of a company can, therefore, be appointed by a simple majority of shareholders and a substantial minority cannot succeed in placing even a single director on board. Section 163 provides opportunity to the minority to place their representatives on the board. This provision enables a company to provide in its articles the system of voting by proportional representation for the appointment of directors. It is devised to make minority votes effective.

4.2.13 Appointment by Board

While the general power to appoint directors is vested in the general meeting of shareholders, there are at least two cases when the board can also appoint new directors. Firstly, articles may empower the directors to appoint additional directors subject to the maximum number fixed therein.

In BN Viswanathan v. Tiffins Baryt Asbestos (P) Ltd. there was conflict between the general meeting and the directorate it was held that at the time of general meeting there was no director validly in office and, therefore, the members had the right to elect.

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24 Section 162 of Companies Act, 2013.
25 Section 152 of Companies Act, 2013.
26 Section 163 of Companies Act, 2013.
27 Section 161 of Companies Act, 2013.
28 AIR 1953 Mad 520: (1953) 1 MLJ 346: (1953) 23 Comp Cas 79.
In *Ram Kissendas Dhanuka v. Satya Charan Law*\(^29\) held that the articles may, however, be so expressed as to delegate the power of appointing new directors to the board to the exclusion of the general meeting.

### 4.2.14 Appointment by the Tribunal

The Company Law Tribunal has power to appoint directors for prevention of oppression and mismanagement.\(^30\) In *Rolta India Ltd. v. Venire Industries Ltd.*\(^31\) an agreement between groups of shareholders not to increase the number of directors and capital of the company and also not to do anything disturbing the existing pattern of management was held to be not binding on the company so as to prevent it from doing any of those things.

### 4.2.15 Director Identification Number

#### 4.2.15.1 Application for allotment of number

Every individual intending to be appointed as director of a company shall make an application for allotment of Director Identification Number to the Central Government in such form and manner and along with such fees as may be prescribed.\(^32\) The Central Government shall, within one month from the receipt of the application under section 153, allot a Director Identification Number to an applicant in such manner as may be prescribed.\(^33\)

#### 4.2.15.2 Prohibition on more than one Identification number

No individual, who has already been allotted a Director Identification Number under section 154, shall apply for, obtain or possess another Director Identification Number.\(^34\)

#### 4.2.15.3 Director to intimate Identification Number

Every existing director shall, within one month of the receipt of Director Identification Number from the Central Government, intimate his Director Identification Number to the company or all companies wherein he is a director.\(^35\)

\(^29\) (1949-50) 77 IA 128: AIR 1950 PC 81. See also, A Ananthalakshmi Ammal v. Indian Trades & Investment Ltd, AIR 1953 Mad 467 and MK Srinivasan v. WS Subramania Iyer, (1932) 32 Comp Cas 147: AIR 1932 Mad 100, where the power of appointment vested in the shareholders, having been usurped by the directors, the appointments were held to be void.

\(^30\) Section 242 (j) of Companies Act, 2013.


\(^32\) Section 153 of Companies Act, 2013.

\(^33\) Section 154 of Companies Act, 2013.

\(^34\) Section 155 of Companies Act, 2013.
4.2.15.4 Company to inform the Registrar of the Number

Every company shall, within fifteen days of the receipt of intimation under section 156, furnish the Director Identification Number of all its directors to the Registrar or any other officer or authority as may be specified by the Central Government with such fees as may be prescribed or with such additional fees as may be prescribed within the time specified under section 403 and every such intimation shall be furnished in such form and manner as may be prescribed.\(^{36}\) If a company fails to furnish Director Identification Number under sub-section (1), before the expiry of the period specified under section 403 with additional fee, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.\(^{37}\)

4.2.15.5 Obligation to indicate Director Identification Number

Every person or company, while furnishing any return, information or particulars as are required to be furnished under this Act, shall mention the Director Identification Number in such return, information or particulars in case such return, information or particulars relate to the director or contain any reference of any director.\(^{38}\)

If any individual or director of a company contravenes any of the provisions of section 152, 155 and 156 he becomes punishable with imprisonment for a term extending up to 6 months or with fine extending up to Rs. 50,000. If default continues further fine of Rs. 500 is levied on daily basis.\(^{39}\)

4.3 Disqualification of Directors

Section 164 lays down the minimum eligibility requirements. A person is not appointed a director in the following cases:

(a) where he is of unsound mind, provided that the fact has been certified by a court of competent jurisdiction and the finding is in force;

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35 Section 156 of Companies Act, 2013.
36 Section 157 (1) of Companies Act, 2013.
37 Section 157 (2) of Companies Act, 2013.
38 Section 158 of Companies Act, 2013.
39 Section 159 of Companies Act, 2013.
(b) where he is an un-discharged insolvent;
(c) where he has applied to be adjudicated as an insolvent and his application is pending;
(d) where he has been sentenced to at least 6 months of or otherwise imprisonment for an offence involving moral turpitude or otherwise, and 5 years have not elapsed from the date of expiry of the sentence. If a person has been convicted of any offence and sentenced in respect thereof to imprisonment for a period of seven years or more, he shall not be eligible to be appointed as a director in any company;
(e) an order for disqualifying him for appointment as a director has been passed by a court or Tribunal and the order is in force;
(f) he has not paid any calls in respect of any shares of the company held by him, whether alone or jointly with others, and six months have elapsed from the last day fixed for the payment of the call;
(g) he has been convicted of the offence dealing with related party transactions under section 188 at any time during the last preceding five years; or
(h) he has not complied with the requirement of Director Identification Number.  

The disqualifications referred to in clauses (d), (e) and (g) of sub-section (1) shall not take effect for thirty days from the date of conviction or order of disqualification; where an appeal or petition is preferred within thirty days as aforesaid against the conviction resulting in sentence or order, until expiry of seven days from the date on which such appeal or petition is disposed off; or where any further appeal or petition is preferred against order or sentence within seven days, until such further appeal or petition is disposed off.  

4.4 Ineligibility for Reappointment

No person who is or has been a director of a company which has not filed financial statements or annual returns for any continuous period of three financial years; or has failed to repay the deposits accepted by it or pay interest thereon or

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40 Section 152 (3) of Companies Act, 2013.
41 Proviso to section 164 of Companies Act, 2013.
to redeem any debentures on the due date or pay interest due thereon or pay any dividend declared and such failure to pay or redeem continues for one year or more, shall be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so.\textsuperscript{42}

### 4.5 Provision for Additional Disqualifications

A private company which is not a subsidiary of a public company may add to further disqualifications.\textsuperscript{43} In \textit{Cricket Club of India v. Madhav L Apte}\textsuperscript{44} it has been held by the Supreme Court that this is an indirect way of saying that a public company and its subsidiary private companies cannot increase the disqualifications or add any other qualifications, such as, for example, that the candidate should be a graduate.

In \textit{Ketan Karkishan Marvadi v. Saurashtra-Kutch Stock Exchange Ltd.}\textsuperscript{45} the restriction on providing for additional disqualification has been held to be not applicable to a Stock Exchange Public Company. Such a company can increase the grounds of disqualification for the membership of a governing council.

### 4.6 Removal of directors

#### 4.6.1 Removal by shareholders

A company may, by ordinary resolution, remove a director before the expiration of his period of office. The English Companies Act, after providing same provision, adds “notwithstanding anything in its (company’s) articles or any agreement between it and him.” These words are not provided in the Indian provision, but same effect would follow as any provision in the company’s articles or in any agreement between a director and the company by which the director is rendered irremovable by an ordinary resolution would be void, being contrary to the Act. This provision intended to do away with arrangements under which directors were either irremovable or removable only by extraordinary resolutions.\textsuperscript{46} Power to remove directors has always been bestowed on

\textsuperscript{42} Section 164 (2) of Companies Act, 2013.
\textsuperscript{43} Section 164 (3) of Companies Act, 2013.
\textsuperscript{44} (1975) 45 Comp Cas 574 (Bom).
shareholders, as we all know that at the end of the day, directors are answerable to shareholders. Nothing has changed in the procedural aspect under Companies Act, 2013 as well. Shareholders can remove any director before the expiry of his tenure, except any director appointed by Tribunal for prevention of oppression and mismanagement\(^{47}\) and a director appointed under principle of proportional representation.\(^{48}\)

Section 115, 169 and deals with the procedure of removal of director by shareholders as follows:

I. **Special Notice To Company**: Only shareholder/s holding not less than 1% of total voting power or holding shares on which an aggregate sum of not less than Rs. 5,00,000 has been paid up as on the date of notice, can send special notice to the Company for removal of director. The same should be signed by the concerned shareholder/s.

II. **Date of meeting**: Above mentioned shareholders have the right to decide the date of meeting. However, the special notice shall be sent not earlier than three months but at least 14 clear days before the date of the meeting\(^{49}\), at which the resolution is to be moved.

III. **Intimation to Director**: The Company shall forthwith send a copy of the notice to the concerned director.

IV. **Reasonable Opportunity of being heard**: The Director may request to send his representations along with the notice to the members and to be heard at the meeting. However, the rights may not be available, if on the application either of the Company or of any other person who claims to be aggrieved, the Tribunal is satisfied that the rights conferred by this sub-section are being abused to secure needless publicity.

V. **Intimation by Company to all shareholders**: Company shall take immediate steps to send the notice to its members, at least 7 clear days

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\(^{47}\) Section 242 of Companies Act, 2013.

\(^{48}\) Section 163 of Companies Act, 2013.

before the meeting. The notice has to be sent in the same manner as in case of any other general meeting of the Company.

VI. **Publication in Newspapers**: If it is not practicable to give the notice as aforementioned, then notice shall be published in English language in English newspaper and in vernacular language in a vernacular newspaper, both having wide circulation in the State where the registered office of the Company is situated. At the same time, the notice shall also be posted on the website, (if any). However, it shall be published at least 7 clear days before the meeting.

VII. **Convening of General Meeting**: Members may pass remove the director by passing ordinary resolution.

VIII. **Appointment of director in place of removed director**: The shareholder/s may recommend appointment of any other director in place of removed director through special notice. Such a director can only hold office till the tenure of removed director.

IX. **Casual Vacancy**: If a new director is not appointed as aforementioned, then Board may fill the position through casual vacancy, however the removed director shall not be re-appointed as a director by Board.

X. **Vacation of Office**: When a director is removed as aforementioned, his office vacates automatically.\(^{50}\)

4.6.2 **Removal by Company Law Tribunal**\(^{51}\)

When, on an application to the Tribunal for prevention of oppression or mismanagement, it finds that a relief ought to be granted, it may terminate or set aside any agreement of the company with a director or managing director or other managerial personnel. When the appointment of a director is so terminated he cannot, except with the leave of the Tribunal, serve any company in a managerial capacity for a period of 5 years.\(^{52}\) It is necessary that the Central Government should be notified of the intention to apply for such leave. This is to enable the

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\(^{50}\) Section 167 of Companies Act, 2013.

\(^{51}\) Section 242 (2) (h) of Companies Act, 2013

\(^{52}\) Section 243(1)(b) of Companies Act, 2013.
Tribunal to hear the Central Government’s point of view on the matter of leave. Neither can he sue the company for damages or compensation for loss of office.\textsuperscript{53}

4.6.3 Resignation by Director

A director may resign from his office by giving a notice in writing to the company. On receiving it, the board has to take notice of the same. The company has then to intimate the Registrar in such manner, within such time and in such form as may be prescribed. The company has to place the fact of such resignation in the report of directors laid in the immediately following general meeting of the company. The director has also to send a copy of his resignation with detailed reasons to the Registrar within 30 days of the resignation in the prescribed manner. The resignation takes effect on the date on which it is received by the company or the date specified in the notice whichever is later.\textsuperscript{54}

4.6.4 Vacation of Office by Directors\textsuperscript{55}

The office of directors is vacated in the following cases:

(a) when he incurs any of the disqualifications specified in section 164;

(b) he absents himself from all the meetings of the Board of Directors held during a period of twelve months with or without seeking leave of absence of the Board;

(c) he acts in contravention of the provisions of section 184 relating to entering into contracts or arrangements in which he is directly or indirectly interested;

(d) he fails to disclose his interest in any contract or arrangement in which he is directly or indirectly interested, in contravention of the provisions of section 184;

(e) he becomes disqualified by an order of a court or the Tribunal;

(f) he is convicted by a court of any offence, whether involving moral turpitude or otherwise and sentenced in respect thereof to imprisonment for not less than six months: Provided that the office shall be vacated by the director even if he has filed an appeal against the order of such court;


\textsuperscript{54} Section 168 of Companies Act, 2013.

\textsuperscript{55} Section 167 of Companies Act, 2013.
(g) he is removed in pursuance of the provisions of this Act;
(h) he, having been appointed a director by virtue of his holding any office or other employment in the holding, subsidiary or associate company, ceases to hold such office or other employment in that company.

A director is obliged at the pain of penalty to leave office when he incurs any of the disqualifications. If a person, functions as a director even when he knows that the office of director held by him has become vacant on account of any of the disqualifications specified in sub-section (1), he shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees, or with both. Where all the directors of a company vacate their offices under any of the disqualifications specified in sub-section (1), the promoter or, in his absence, the Central Government shall appoint the required number of directors who shall hold office till the directors are appointed by the company in the general meeting. A private company may, by its articles, provide any other ground for the vacation of the office of a director in addition to those specified in sub-section (1).

4.7 Powers of Directors

The Board of Directors of a company shall be entitled to exercise all such powers, and to do all such acts and things, as the company is authorised to exercise and do provided that Board shall be subject to the provisions contained in that behalf in this Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made there under, including regulations made by the company in general meeting. It is further provided that the Board shall not exercise any power or do any act or thing which is directed or required, whether under this Act or by the memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting. The Board of Directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at meetings of the Board, namely:-

i. to make calls on shareholders in respect of money unpaid on their shares;
ii. to authorise buy-back of securities under section 68;

56 Section 179 of Companies Act, 2013.
iii. to issue securities, including debentures, whether in or outside India;

iv. to borrow moneys;

v. to invest the funds of the company;

vi. to grant loans or give guarantee or provide security in respect of loans;

vii. to approve financial statement and the Board’s report;

viii. to diversify the business of the company;

ix. to approve amalgamation, merger or reconstruction;

x. to take over a company or acquire a controlling or substantial stake in another company;

xi. any other matter which may be prescribed.

Some of the powers\textsuperscript{57} are to be exercised by the board only with the consent of the company by a special resolution namely:

i. To sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company or where the company owns more than one undertaking, of the whole or substantially the whole of any of such undertakings.

ii. To invest otherwise in trust securities the amount of compensation received by it as a result of any merger or amalgamation;

iii. To borrow money, where the money to be borrowed, together with the money already borrowed by the company will exceed aggregate of its paid-up share capital and free reserves, apart from temporary loans obtained from the company’s bankers in the ordinary course of business: Provided that the acceptance by a banking company, in the ordinary course of its business, of deposits of money from the public, repayable on demand or otherwise, and withdraw able by cheque, draft, order or otherwise, shall not be deemed to be a borrowing of moneys by the banking company within the meaning of this clause.

\textsuperscript{57} Section 180 of Companies Act, 2013.
iv. To remit, or give time for the repayment of, any debt due from a director.58

4.8 Duties of Directors

The duties and responsibilities of directors stipulated by the Indian Companies Act of 2013 can broadly be classified into the following two categories:

i. The duties and liabilities which encourage and promote the sincerest investment of the best efforts of directors in the efficient and prudent corporate management, in providing elegant and swift resolutions of various business-related issues including those which are raised through "red flags", and in taking fully mature and wise decisions to avert unnecessary risks to the company.

ii. Fiduciary duties which ensure and secure that the directors of companies always keep the interests of the company and its stakeholders, ahead and above their own personal interests.

The Companies Act, 2013 has in section 166 made a statutory formulation of director’s duties. They are mentioned as follows:

I. Director to act in accordance with articles of the company.

II. A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.

III. A director of a company shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment.

IV. A director of a company shall not involve in a situation in which he may have a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the company.

V. A director of a company shall not achieve or attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates and if such director is found guilty of making any undue gain, he shall be liable to pay an amount equal to that gain to the company.

VI. A director of a company shall not assign his office and any assignment so made shall be void.

4.9 Liabilities of Directors

The ubiquitous issue of corruption and the high risk of internal fraud raise serious concerns about the liability of corporate directors. Director liability in India can be divided into two principal areas: (1) liability under the Companies Act of 1956 (the 1956 Act), which has now transitioned to the Companies Act of 2013 (the 2013 Act); and (2) liability under other Indian statutes. There has been a seminal shift in the Indian corporate legal regime with the enactment of the 2013 Act and more recent amendments. For instance, penalties under the 1956 Act that were seen as ineffective have been significantly amplified under the 2013 Act. The 2013 Act also provides statutory recognition to the duties of a director, such as exercise of due and reasonable care, skill, diligence, and independent judgment.

One of the key concepts of the Companies Act is the meaning of the term “officer who is in default.” Under the act, liability for default by a company has been imposed on an officer who is in default. By virtue of their positions in the company, the managing director, the whole-time director, and the company secretary directly fall within the scope of this term. Under the 1956 Act, certain key employees such as the chief executive officer and chief financial officer did not directly come within the ambit of the term, which raised serious concerns because these personnel were viewed as key officials in any company. The 2013 Act corrects this anomaly and significantly expands the scope of the expression “officer in default.” The term also includes the following:

1. Any individual who, under the superintendence, control, and direction of the board of directors, exercises the management of the whole, or substantially the whole, of the affairs of a company;
2. Any person on whose advice, directions, or instructions the board of directors is accustomed to act, other than persons giving advice in a professional capacity; and

3. Every director aware of wrongdoing by virtue of knowledge of or participation in proceedings of the board without objection.

A critical failure of Indian corporate law was further highlighted during various corporate and financial scams, such as the Harshad Mehta episode or the Satyam fiasco. To address this issue, the 2013 Act now specifically defines “fraud” and states that a person who is guilty of it may be punished by imprisonment for up to 10 years, and where fraud involves the public interest, the minimum sentence prescribed is three years. Fraud, as defined under Companies Act, 2013, includes any act or abuse of position committed with intent to deceive, to gain undue advantage from, or to injure the interests of a person, company, shareholders, or creditors, whether or not there is wrongful gain or loss.\(^{59}\)

### 4.9.1 Shareholder Disputes

In the context of various shareholder disputes, the increased liability under the 2013 Act could be a useful tool to increase pressure on defaulting directors, nominating shareholders, or promoters. In addition, while resignation may protect a director from subsequent defaults, an erstwhile director may still continue to be liable for any defaults that took place during his or her tenure\(^{60}\), as now clarified under the Act. The 2013 changes to the act prompted concerns about the role, accountability, and responsibility of nonexecutive, nominee, and independent directors, who could be caught on the wrong side of the company’s disputes. Under the 2013 Act, an independent director or a nonexecutive director can be held liable under the 2013 Act only for acts of omission or commission by a company that occurred with the director’s knowledge attributable through board processes and the director’s consent or connivance or where he or she failed to act diligently.\(^{61}\) This, to a certain extent, alleviates the concern surrounding independent director liability. However, questions such as whether a director acted

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\(^{59}\) Section 447 of the Companies Act, 2013.  
\(^{60}\) Section 168(2) of the Companies Act, 2013.  
\(^{61}\) Section 150(12) of the Companies Act, 2013.
diligently and whether knowledge could be attributed to a director by mere presence at board meetings still remain unanswered. Moreover, liability faced by independent and nominee directors under various other enactments remains a legitimate concern. Directors may also face liability under other Indian laws. Such liability may not always be foreseeable, and actions such as the dishonour of checks, offenses under the Income Tax Act of 1961, violation of foreign exchange regulations, breach of securities regulations, non-payment of provident fund contributions, violation of the Shops and Establishments Act, or food adulteration could result in liability that may not always be limited to the executive directors. In addition, some statutes do not distinguish between executive and non-executive directors or base liability on the role a particular director was performing on the company’s board. Consequently, liability may be difficult to foresee or predict. While it is difficult to provide any particular standard that will determine an individual’s exposure to liability, a person will generally be held liable for wrongdoing committed by a company if he or she falls into either of the following categories: 1. any person who, at the time the offense was committed, was in charge of and responsible to the company for the conduct of its business; or 2. any director, manager, secretary, or other officer of the company: a. with whose consent and connivance the offense was committed, or b. whose negligence resulted in the offense. The Indian Supreme Court has, in this context, ruled that a managing director is prima facie in charge of and responsible for the company’s business and can be prosecuted for misdeeds by the company. But only those officers of the company who fall within the scope of the definition “officer who is in default” are covered. A simple averment in a complaint that a director was in charge of and responsible for the conduct of the business of the company is sufficient to state a claim against an officer who is in default. In cases of fraud, it may be difficult to have a clear line of demarcation as to whether the director could have prevented the fraud if he or she had used due diligence. While the role of non-executive directors may consist of providing strategic guidance, this more limited status may not protect them from liability. Nor will being a nonparticipant

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at board meetings. The law now requires directors to adopt an inquisitive approach and question the company’s background information, how it was obtained, and the decisions that are taken based on such information. With increasing global interest in Indian companies and a changing legal landscape, new players will continue to enter the domain unaware of the possible consequences. Consequently, director indemnification clauses in shareholder and director agreements should be cautiously and thoroughly negotiated. Directors’ and officers’ liability insurance is also a tool that is becoming increasingly popular in India. Such insurance and indemnification should sufficiently cover the director even after resignation. The Indian economy presents myriad and growing opportunities, but would be corporate directors and their lawyers should tread carefully. Rapidly modernizing laws on director and officer liability require their full attention.63

4.9.2 Liabilities of a Director:

4.9.2.1 Financial statement

Financial statements to give a true and fair view of the state of affairs of the company, complying with the accounting standards notified under section 133 and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III. Provided that the items contained in such financial statements shall be in accordance with the accounting standards.64 If a company contravenes the provisions of this section, the managing director, the whole-time director in charge of finance, the Chief Financial Officer or any other person charged by the Board with the duty of complying with the requirements of this section and in the absence of any of the officers mentioned above, all the directors shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.65

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64 Section 129 of the Companies Act, 2013.
65 Section 129 (7) of the Companies Act, 2013.
Failure to attach to balance sheet a report of the Board of directors and statement on declaration given by independent directors. If the company contravenes the provisions of the Act, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

4.9.2.2 Register of directors and key managerial personnel and their shareholding

Every company shall keep at its registered office a register containing such particulars of its directors and key managerial personnel as may be prescribed, which shall include the details of securities held by each of them in the company or its holding, subsidiary, subsidiary of company’s holding company or associate companies. A return containing such particulars and documents as may be prescribed, of the directors and the key managerial personnel shall be filed with the Registrar within thirty days from the appointment of every director and key managerial personnel, as the case may be, and within thirty days of any change taking place. If a company contravenes the provisions, the company and every officer of the company who is in default shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees.

4.9.2.3 Failure to disclose interest in a contract or arrangement

Any director or any other employee of a company, who had entered into or authorised the contract or arrangement in violation of the provisions of this section shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees.

4.9.2.4 False declaration of company's solvency

Any director of a company making a declaration under this section without having reasonable grounds for the opinion that the company will be able to pay its

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66 Section 134 (3) of the Companies Act, 2013.
67 Section 134 (8) of the Companies Act, 2013.
68 Section 170 of the Companies Act, 2013.
69 Section 172 of the Companies Act, 2013.
70 Section 184 of the Companies Act, 2013.
71 Section 305 of the Companies Act, 2013.
debts in full from the proceeds of assets sold in voluntary winding up shall be punishable with imprisonment for a term which shall not be less than three years but which may extend to five years or with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees, or with both.72

4.9.3 Liability of non-executive / Independent Directors

An independent director and a non-executive director not being promoter or key managerial personnel, shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

4.9.3.1 Reduction of Capital

If any officer of the company-

(a) knowingly conceals the name of any creditor entitled to object to the reduction;

(b) knowingly misrepresents the nature or amount of the debt or claim of any creditor; or

(c) abets or is privy to any such concealment or misrepresentation as aforesaid, he shall be liable under section 447.73

4.9.3.2 Proxies

If for the purpose of any meeting of a company, invitations to appoint as proxy a person or one of a number of persons specified in the invitations are issued at the company’s expense to any member entitled to have a notice of the meeting sent to him and to vote thereat by proxy, every officer of the company who knowingly issues the invitations as aforesaid or wilfully authorises or permits their issue shall be punishable with fine which may extend to one lakh rupees. Provided that an officer shall not be punishable under this sub-section by reason only of the issue to a member at his request in writing of a form of appointment naming the proxy, or of a list of persons willing to act as proxies, if the form or

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73 Section 66 (10) of the Companies Act, 2013.
list is available on request in writing to every member entitled to vote at the meeting by proxy.  

4.9.3.3 Meetings of Board

Every officer of the company whose duty is to give notice under this section and who fails to do so shall be liable to a penalty of twenty-five thousand rupees.

4.9.3.4 Secretarial Audit

If a company or any officer of the company or the company secretary in practice, contravenes the provisions of this section, the company, every officer of the company or the company secretary in practice, who is in default, shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

4.9.3.5 Conduct of Inspection and Enquiry

If any director or officer of the company disobeys the direction issued by the Registrar or the inspector under this section, the director or the officer shall be punishable with imprisonment which may extend to one year and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

If a director or an officer of the company has been convicted of an offence under this section, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company.

4.9.3.6 Inspection by Serious Fraud Investigation Officer

On receipt of the investigation report, the Central Government may, after examination of the report (and after taking such legal advice, as it may think fit), direct the Serious Fraud Investigation Office to initiate prosecution against the company and its officers or employees, who are or have been in employment of the company or any other person directly or indirectly connected with the affairs.

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74 Section 105 (5) of the Companies Act, 2013.
75 Section 173 (4) of the Companies Act, 2013.
76 Section 204 (4) of the Companies Act, 2013.
77 Section 207 (4) of the Companies Act, 2013.
Notwithstanding anything contained in this Act or in any other law for the time being in force, the investigation report filed with the Special Court for framing of charges shall be deemed to be a report filed by a police officer under section 173 of the Code of Criminal Procedure, 1973 of the company.\textsuperscript{78}

4.9.3.7 Directions for filing statement of Affairs – Winding Up by Tribunal

If any director or officer of the company contravenes the provisions of this section, the director or the officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both.\textsuperscript{79}

4.9.3.8 Liability as “Officer in Default”

I. Directors are liable as officers in default under all sections where specific penalty is provided for each officer in default.

II. Where no specific penalty is provided under the Act, they are liable under Section 450.

4.9.3.9 Liability for Fraud

“Fraud” in relation to affairs of a company or any body corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss;

Any person who is found to be guilty of fraud, shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud.

4.9.3.10 Personal Liability

I. Directors can be made personally liable if

\textsuperscript{78} Section 212 of the Companies Act, 2013.

\textsuperscript{79} Section 274 (4) of the Companies Act, 2013.
a) When the directors enter into contract in their own name.
b) When they enter into contracts on behalf of company but fail to use “LTD. Or PVT LTD.”
c) When directors exceed their powers
d) The Board of Directors should act an agent of company, not of a single director. Therefore a single director cannot enter into a contract on behalf of company unless the Board of Directors authorises.

II. Civil Liability for misstatement in prospectus

Where it is proved that a prospectus has been issued with intent to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person concerned shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.  

III. Damages for Fraud

Where a company fails to repay the deposit or part thereof or any interest thereon referred to in section 74 within the time specified in sub-section (1) of that section or such further time as may be allowed by the Tribunal under sub-section (2) of that section, and it is proved that the deposits had been accepted with intent to defraud the depositors or for any fraudulent purpose, every officer of the company who was responsible for the acceptance of such deposit shall, without prejudice to the provisions contained in subsection (3) of that section and liability under section 447, be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by the depositors.  

IV. Liability for fraudulent conduct of business

If in the course of the winding up of a company, it appears that any business of the company has been carried on with intent to defraud

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80 Section 35 of the Companies Act, 2013.
81 Section 75 of the Companies Act, 2013.
creditors of the company or any other persons or for any fraudulent purpose, the Tribunal, on the application of the Official Liquidator, or the Company Liquidator or any creditor or contributory of the company, may, if it thinks it proper so to do, declare that any person, who is or has been a director, manager, or officer of the company or any persons who were knowingly parties to the carrying on of the business in the manner aforesaid shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Tribunal may direct.  

4.10 Committees to be constituted under Act

With an eye on improving corporate governance the new Companies Act, 2013 mandates a number of board committees for specified companies for audit, nomination and remuneration, corporate social responsibility and stakeholder’s relationship. According to this Act the following committees are to be formed by a company-

4.10.1 Audit Committee

The Companies Act provides for the formation of Audit Committee. This is not the new concept. This has been available in the erstwhile Companies Act, 1956. An Audit Committee was required for every public company whose paid up capital was Rs. 5 crore or more. The Companies Act provides that the Board of Directors of every listed company and such other class or classes of company, as may be prescribed, shall constitute an Audit Committee. Every Audit Committee of a company existing immediately before the commencement of this Act shall, within one year of such commencement, be reconstituted in accordance with this Act. The majority of members of Audit Committee including its Chairperson shall be persons with ability to read and understand the financial statement. The act provides that the Audit Committee shall consist of a minimum of three directors with independent directors forming a majority.

4.10.1.1 Functions

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82 Section 339 of the Companies Act, 2013.
83 Section 177 of the Companies Act 2013.
84 Section 292 A of the Companies Act, 1956.
85 Section 177 (2) of the Companies Act 2013.
Every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall include:

I. The recommendation for appointment, remuneration and terms of appointment of auditors of the company;

II. Review and monitor of the auditor’s independence and performance and effectiveness of audit process;

III. Examination of the financial statement and the auditors’ report thereon;

IV. Approval of any subsequent modification of transaction of the company with related parties;

V. Scrutiny of inter-corporate loans and investments;

VI. Valuation of undertakings or assets of the company, wherever it is necessary;

VII. Evaluation of internal financial controls and risk management systems;

VIII. Monitoring the end use of funds raised through public offers and related matters.\(^{86}\)

4.10.1.2 **Powers**

The Audit Committee may call for the comments of the auditors about internal control systems, the scope of audit, including the observations of the auditors and review of financial statement before their submission to the Board and may also discuss any related issues with internal and statutory auditors and the management of the company.\(^{87}\) The Audit Committee shall have authority to investigate into any matter in relation to the functions or referred to it by the Board and for this purpose shall have powers to obtain professional advice from external sources and have full access to information contained in the records of the company.\(^{88}\)

4.10.1.3 **Rights of Auditors**

The Auditors of a company and the key managerial personnel shall have a right to be heard in the meetings of the Audit Committee when it considers the Auditor’s report but shall not have the right to vote.\(^{89}\)

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\(^{86}\) Section 177 (4) of the Companies Act 2013.

\(^{87}\) Section 177 (5) of the Companies Act 2013.

\(^{88}\) Section 177 (6) of the Companies Act 2013.

\(^{89}\) Section 177 (7) of the Companies Act 2013.
4.10.1.4 Disclosure in Board’s report

The Board’s report shall disclose the composition of an Audit Committee and where the Board had not accepted any recommendation of the Audit Committee, the same shall be disclosed in such report along with the reasons therefore.90

4.10.1.5 Contravention

In case of any contravention of the provisions of section 177 and this section, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees, or with both.91

4.10.2 Nomination and Remuneration Committee

The Companies Act provides for the constitution of nomination and remuneration committee. According to the provisions of the act the Board of Directors of every listed company; and such other class or classes of companies as may be prescribed shall constitute the Nomination and Remuneration Committee consisting of 3 or more non executive directors out of which of which not less than one half shall be independent directors. The Chair person of the company, whether executive or non executive, may be appointed as a member of the said committee but shall not chair such Committee.92

4.10.2.1 Functions

I. The Committee shall identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, recommend to the Board their appointment and removal and shall carry out evaluation of every director’s performance.93

II. The Committee shall formulate the criteria for determining qualifications, positive attributes and independence of a director and recommend to the

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90 Section 177 (8) of the Companies Act 2013.
91 Section 178 (8) of the Companies Act 2013.
92 Section 178 (1) of the Companies Act 2013.
93 Section 178 (2) of the Companies Act 2013.
Board a policy, relating to remuneration for the directors, key managerial personnel and other employees;  

III. The Committee shall, while formulating the policy shall ensure that-

a. The level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required to run the company successfully;

b. Relationship of remuneration to performance is clear and meets appropriate performance benchmarks; and

c. Remuneration to directors, key managerial personnel and senior management involves a balance between fixed and incentive pay reflecting short and long term performance objectives appropriate to the working of the company and its goals.

Such policy shall be disclosed in the Board’s report. The term ‘senior management’ means personnel of the company who are members of its core management team excluding Board of Directors comprising all members of management one level below the executive directors, including the functional heads. The Chairperson of this committee or in his absence, any other member of the committee authorized by him in this behalf shall attend the general meetings of the company.

4.10.3 Stakeholders Relationship Committee

The provisions of the Act provides that the Board of Directors of a company, which consists of more than 1000 shareholders, debenture holders, deposit holders and any other security holders at any time during a financial year shall constitute a Stakeholders Relationship Committee. The said committee shall consist of a chairperson who shall be a non executive director and such other members as may be decided by the Board.

The Committee shall consider and resolve the grievances of security holders of the company. The Chairperson of this committee or in his absence,

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94 Section 178 (3) of the Companies Act 2013.
95 Section 178 (4) of the Companies Act 2013.
96 Section 178 (5) of the Companies Act 2013.
97 Section 178 (6) of the Companies Act 2013.
any other member of the committee authorized by him in this behalf shall attend
the general meetings of the company.  

Non-consideration of resolution of any grievance by the Stakeholders
Relationship Committee in good faith shall not constitute a contravention of this
section.

4.10.4 Corporate and Social Responsibility Committee

The Companies Act provides for the constitution of Corporate and Social
Responsibility Committee. According to this Act, every company having net
worth of Rs.500 crores or more, or turnover of Rs.1000 crores or more or a net
profit of Rs.5 crores or more during any financial year shall constitute a Corporate
Social Responsibility Committee of the Board consisting of three or more
directors, out of which at least one director shall be an independent director.
The Board’s report shall disclose the composition of the Corporate Social
Responsibility Committee.

4.10.4.1 Functions

The Corporate Social Responsibility Committee shall formulate and
recommend to the Board, a Corporate Social Responsibility Policy which shall
indicate the activities to be undertaken by the company as specified in Schedule
VII, as detailed below:

I. Activities relating to-
   a) Eradicating extreme hunger and poverty;
   b) Promotion of education;
   c) Promoting gender equality and empowering women;
   d) Reducing child mortality and improving maternal health;
   e) Combating human immune deficiency virus, acquired immuno
deficiency syndrome, malaria and other diseases;
   f) Ensuring environmental sustainability;
   g) Employment enhancing vocational skills;

98 Section 178 (7) of the Companies Act 2013.
99 Section 135 of the Companies Act 2013.
100 Section 135 (1) of the Companies Act 2013.
101 Section 135(2) of the Companies Act 2013.
h) Social business projects;
i) Contributions to Prime Minister’s National Relief Fund or any other fund set up by the Central Government of the State Government for socio-economic development and relief and funds for the welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women; and
j) Such other matters as may be prescribed.

II. Recommend the amount of expenditure to be incurred on the activities for above; and

III. Monitor the Corporate Social Responsibility Policy of the company from time to time.

4.10.4.2 Obligations of the Board

The Board of every company shall after taking into account the recommendations of the Committee approve the Corporate Social Responsibility Policy for the company and disclose contents of such policy in its report and also place it on the company’s website, if any, in such manner, as may be prescribed and ensure that the activities as are included in the Policy of the company are undertaken by the company.\textsuperscript{102}

The Board shall ensure that the company spends, in every financial year, at least 2\% of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its policy. The company shall give preference to the local area and areas around it where it operates, for spending the amount earmarked for Corporate Social Responsibility activities. If the company fails to spend such amount, the Board shall, in its report specify the reasons for not spending the amount.\textsuperscript{103}

4.10.5 Appointment of Committees

Section 315 provides for the appointment of committee. According to this section where there are no creditors of a company, such company in its general meeting and, where a meeting of creditors is held under section 306, such

\textsuperscript{102} Section 135 (4) of the Companies Act 2013.
\textsuperscript{103} Section 135 (5) of the Companies Act 2013.
creditors, as the case may be, may appoint such committees as considered appropriate to supervise the voluntary liquidation and assist the Company Liquidator in discharging his or its functions.\textsuperscript{104}

4.11 Meetings of the Board

The way we run board meetings says a lot about how we run the company. Successful companies use board meetings to create and improve key business strategies. The board of directors of a company is primarily an oversight board. It oversees the management of the company to ensure that the interest of non-controlling shareholders is protected. It also functions as advisory board. Independent directors bring diverse knowledge and expertise in the board room and the CEO uses the knowledge pool in addressing issues being faced by the company. The most important function of a monitoring board is to provide direction to the company. Another very important function of a monitoring board is to set the ‘tone at the top’. It is expected to create the right culture within the company.

Every company shall hold the first meeting of the Board of Directors within thirty days of the date of its incorporation and thereafter hold a minimum number of four meetings of its Board of Directors every year in such a manner that not more than one hundred and twenty days shall intervene between two consecutive meetings of the Board, Provided that the Central Government may, by notification, direct that the provisions of this sub-section shall not apply in relation to any class or description of companies or shall apply subject to such exceptions, modifications or conditions as may be specified in the notification.\textsuperscript{105}

The participation of directors in a meeting of the Board may be either in person or through video conferencing or other audio visual means, as may be prescribed, which are capable of recording and recognising the participation of the directors and of recording and storing the proceedings of such meetings along with date and time, Provided that the Central Government may, by notification,


\textsuperscript{105} Section 173(1) of the Companies Act 2013.
specify such matters which shall not be dealt with in a meeting through video conferencing or other audio visual means.\textsuperscript{106}

A meeting of the Board shall be called by giving not less than seven days’ notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means, Provided that a meeting of the Board may be called at shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be present at the meeting. Provided further that in case of absence of independent directors from such a meeting of the Board, decisions taken at such a meeting shall be circulated to all the directors and shall be final only on ratification thereof by at least one independent director, if any.\textsuperscript{107} Every officer of the company whose duty is to give notice under this section and who fails to do so shall be liable to a penalty of twenty-five thousand rupees.\textsuperscript{108}

A One Person Company, small company and dormant company shall be deemed to have complied with the provisions of this section if at least one meeting of the Board of Directors has been conducted in each half of a calendar year and the gap between the two meetings is not less than ninety days, Provided that nothing contained in this sub-section and in section 174 shall apply to One Person Company in which there is only one director on its Board of Directors.\textsuperscript{109}

\textbf{4.11.1 Quorum Required For Board Meetings}

The quorum for a meeting of the Board of Directors of a company is one-third of its total strength or two directors, whichever is higher, and the participation of the directors by video conferencing or by other audio visual means shall also be counted for the purposes of quorum.\textsuperscript{110} The continuing directors may act notwithstanding any vacancy in the Board; but, if and so long as their number is reduced below the quorum fixed by the Act for a meeting of the Board, the continuing directors or director may act for the purpose of increasing the number of directors to that fixed for the quorum, or of summoning a general meeting of

\begin{footnotes}
\item[106] Section 173 (2) of the Companies Act 2013.
\item[107] Section 173 (3) of the Companies Act 2013.
\item[108] Section 173 (4) of the Companies Act 2013.
\item[109] Section 173 (5) of the Companies Act 2013.
\item[110] Section 174 of the Companies Act, 2013.
\end{footnotes}
the company and for no other purpose. But where this quorum cannot be formed, because of the interested directors, then the number of directors who are not interested, being not less than two, shall be the quorum. If a meeting cannot be held for want of quorum, it stands adjourned till the same day in the next week. In *North Eastern Insurance Co. Ltd., Re* the Calcutta High Court held that the directors can fix a time for reassembling and no further notice is necessary. In the case allotment of debentures of two directors, being resolved upon with the help of an interesting director was held void.

In *Hood Sialmakers Ltd. v. Axford* this case it was held that quorum requirement does not become dispensed with because one out of two directors is abroad. A meeting attended by only one director was held not to be valid.

In *Pradeep Kumar Banerjee v. Union of India* this case it was held that if articles of a company provides for a total number of 15 directors but at the material time only 6 directors were in office, the quorum meant 1/3 of the 6 directors and therefore, a meeting attended by 2 directors only was valid.

### 4.11.2 Passing of resolution

No resolution shall be deemed to have been duly passed by the Board or by a committee thereof by circulation, unless the resolution has been circulated in draft, together with the necessary papers, if any, to all the directors, or members of the committee, as the case may be, at their addresses registered with the company in India by hand delivery or by post or by courier, or through such electronic means as may be prescribed and has been approved by a majority of the directors or members, who are entitled to vote on the resolution. Provided that, where not less than one-third of the total number of directors of the company for the time being require that any resolution under circulation must be decided at a meeting, the chairperson shall put the resolution to be decided at a meeting of the Board.

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111 Section 174 (2) of the Companies Act, 2013
112 Section 174(4) of the Companies Act, 2013
113 (1919) 1 Ch 198: 120 LT 223. See also, Pramod Kumar Mittle v. Southern Steel Ltd, (1980) 50 Comp Cas 555 (Cal).
114 (1997) 1 BCLC 721 (QBD).
116 Section 175 (1) of Companies Act, 2013.
4.11.3 Defects in appointment of directors not to invalidate actions taken

No act done by a person as a director shall be deemed to be invalid, notwithstanding that it was subsequently noticed that his appointment was invalid by reason of any defect or disqualification or had terminated by virtue of any provision contained in this Act or in the articles of the company, Provided that nothing in this section shall be deemed to give validity to any act done by the director after his appointment has been noticed by the company to be invalid or to have terminated.¹¹⁷

4.12 Overall Managerial Remuneration

Regulation and control over director’s remuneration becomes necessary for several reasons prominent among them being prevention of diversion of corporate funds for personal use and the impact which an unduly high executive reward has upon the rest of the society. The total managerial remuneration payable by a public company, to its directors, including managing director and whole-time director, and its manager in respect of any financial year shall not exceed 11% of the net profits of that company for that financial year computed in the manner laid down in section 198 except that the remuneration of the directors shall not be deducted from the gross profits. Provided that the company in general meeting may, with the approval of the Central Government, authorise the payment of remuneration exceeding 11% of the net profits of the company, subject to the provisions of Schedule V. Provided further that, except with the approval of the company in general meeting, the remuneration payable to any one managing director; or whole-time director or manager shall not exceed 5% of the net profits of the company and if there is more than one such director remuneration shall not exceed 10% of the net profits to all such directors and manager taken together. The remuneration payable to directors who are neither managing directors nor whole-time directors shall not exceed 1% of the net profits of the company, if there is a managing or whole-time director or manager, 3% of the net profits in

¹¹⁷ Section 176 of Companies Act, 2013.
any other case. The percentages aforesaid shall be exclusive of any fees payable to directors under sub-section (5).

If, in any financial year, a company has no profits or its profits are inadequate, the company shall not pay to its directors, including any managing or whole-time director or manager, by way of remuneration any sum exclusive of any fees payable to directors under sub-section (5) hereunder except in accordance with the provisions of Schedule V and if it is not able to comply with such provisions, with the previous approval of the Central Government.

The remuneration payable to the directors of a company, including any managing or whole-time director or manager, shall be determined, in accordance with and subject to the provisions of this section, either by the articles of the company, or by a resolution or, if the articles so require, by a special resolution, passed by the company in general meeting and the remuneration payable to a director determined aforesaid shall be inclusive of the remuneration payable to him for the services rendered by him in any other capacity: Provided that any remuneration for services rendered by any such director in other capacity shall not be so included if the services rendered are of a professional nature and in the opinion of the Nomination and Remuneration Committee, if the company is covered under sub-section (1) of section 178, or the Board of Directors in other cases, the director possesses the requisite qualification for the practice of the profession. A director may receive remuneration by way of fee for attending meetings of the Board or Committee thereof or for any other purpose whatsoever as may be decided by the Board: Provided that the amount of such fees shall not exceed the amount as may be prescribed: Provided further that different fees for different classes of companies and fees in respect of independent director may be such as may be prescribed. A director or manager may be paid remuneration either by way of a monthly payment or at a specified percentage of the net profits

118 Section 197 (1) of Companies Act, 2013.
119 Section 197 (2) of Companies Act, 2013.
120 Section 197 (3) of Companies Act, 2013.
121 Section 197 (4) of Companies Act, 2013.
122 Section 197 (5) of Companies Act, 2013.
of the company or partly by one way and partly by the other.\textsuperscript{123} Notwithstanding anything contained in any other provision of this Act but subject to the provisions of this section, an independent director shall not be entitled to any stock option and may receive remuneration by way of fees provided under sub-section (5), reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members.\textsuperscript{124} If any director draws or receives, directly or indirectly, by way of remuneration any such sums in excess of the limit prescribed by this section or without the prior sanction of the Central Government, where it is required, he shall refund such sums to the company and until such sum is refunded, hold it in trust for the company.\textsuperscript{125} Every listed company shall disclose in the Board’s report, the ratio of the remuneration of each director to the median employee’s remuneration and such other details as may be prescribed.\textsuperscript{126} Subject to the provisions of this section, any director who is in receipt of any commission from the company and who is a managing or whole-time director of the company shall not be disqualified from receiving any remuneration or commission from any holding company or subsidiary company of such company subject to its disclosure by the company in the Board’s report.\textsuperscript{127}

\textbf{4.12.1 Penalty}

If any person contravenes the provisions of this section, he shall be punishable with fine which shall not be less than Rs 1,00,000 but extending up to Rs 5,00,000.\textsuperscript{128}

\textbf{4.12.2 Recovery of Remuneration in Certain Cases}

Without prejudice to any liability incurred under the provisions of this Act or any other law for the time being in force, where a company is required to restate its financial statements due to fraud or non-compliance with any requirement under this Act and the rules made thereunder, the company shall recover from any past or present managing director or whole-time director or manager or Chief Executive Officer (by whatever name called) who, during the period for which the

\textsuperscript{123} Section 197 (6) of Companies Act, 2013.
\textsuperscript{124} Section 197 (7) of Companies Act, 2013.
\textsuperscript{125} Section 197 (9) of Companies Act, 2013.
\textsuperscript{126} Section 197 (12) of Companies Act, 2013.
\textsuperscript{127} Section 197 (14) of Companies Act, 2013.
\textsuperscript{128} Section 197 (15) of Companies Act, 2013.
financial statements are required to be re-stated, received the remuneration (including stock option) in excess of what would have been payable to him as per restatement of financial statements.\textsuperscript{129}

4.12.3 Central Government or Company to fix limit with regard to Remuneration

Irrespective of the provisions of the Act, the Central Government or the company, while granting approval under section 196 or to any appointment or remuneration under section 197 in the context of a company with no or inadequate profits, while fixing the remuneration regard has be had to the financial position of the company, the remuneration or commission drawn by the individual concerned in any other capacity, the remuneration or commission drawn by him from any other company, professional qualifications and experience of the individual concerned and such other matters as may be prescribed.\textsuperscript{130}

4.13 Appointment of Key Managerial Personnel

The companies Act, 2013, provide that certain specified companies, as may be prescribed by rules, shall have following whole-time key managerial personnel\textsuperscript{131}:-

I. MD, CEO, Manager or Whole-Time Director

II. Company Secretary

III. CFO

Every listed company and every other company, whether public or private, having paid up share capital of Rs.5 cr. more should have whole-time Key Management Personnel. It is also provided in that, unless the articles of the Company provide otherwise, or the company does not carry on multiple businesses an individual shall not be the Chairperson as well as MD or CEO at the same time. Further, it is provided that every whole-time Key Management Personnel shall be appointed by a resolution of the Board containing terms and conditions of appointment and remuneration. Such Key Management Personnel shall not hold office in more than one Company, except in its subsidiary at the

\textsuperscript{129} Section 199 of Companies Act, 2013.
\textsuperscript{130} Section 200 of Companies Act, 2013.
\textsuperscript{131} Section 203 of the Companies Act, 2013.
same time. However, he can be a director in any company with the permission of the Board. If any Key Management Personnel is holding such position in more than one company at the time of commencement of the New Act, he will have to select one of the Companies within 6 months of such commencement. The company may appointment a Managing Director who is already Managing Director or Manager of one or more companies. Such appointment will have to be approved by the Board by a resolution to be passed at its meeting and should be approved by all the Directors present at the meeting. Specific notice giving details of such proposal should be given for such Board Meeting. If office of such Key Management Personnel is vacated, it should be filled up by the Board within 6 months.\textsuperscript{133}

In the event of contravention of this section the following penal action can be taken. The company will be punishable with minimum fine of Rs. one lakh which may extend to Rs.5 lakhs. Every defaulting director or Key Management Personnel will be punishable with fine up to Rs.50000. In the event of continuing default, further fine upto Rs.1000/- for every day during which the contravention continues can be levied.\textsuperscript{134}

\subsection*{4.13.1 Secretarial Audit:}

Every listed company and a company belonging to other class of companies as may be prescribed shall annex with its Board’s report made in terms of sub-section (3) of section 134, a secretarial audit report, given by a company secretary in practice, in such form as may be prescribed. If there are any qualifications, observation and other remarks in the above report, the Board will have to give explanation about the same in the Board report as provided in section 134(3). If the company, any officer or Company Secretary in practice contravenes this section the defaulting person shall be liable to punishment by way of minimum fine of Rs.1 lakh which may extend to Rs.5 lakhs. Section 204 shall apply to a listed company and every public company having paid up share capital of Rs.100 crore or more.\textsuperscript{135}

\textsuperscript{132} Section 203 (3) of the Companies Act, 2013.
\textsuperscript{133} Section 203 (4) of the Companies Act, 2013.
\textsuperscript{134} Section 203 (5) of the Companies Act, 2013.
\textsuperscript{135} Section 204 of the Companies Act, 2013.
4.13.2 Functions of Company Secretary

The functions of the Company Secretary are as under:

I. To report to the Board about compliance with the provisions of the Act, the Rules and other applicable Laws.

II. To ensure that the company complies with the applicable Secretarial standards issued by the Institute of Company Secretaries of India.

III. To discharge such other duties as may be prescribed. (Refer Draft Rule 13.8 for list of duties to be performed by a Company Secretary).

For the purpose of this section, the expression “secretarial standards” means secretarial standards issued by the Institute of Company Secretaries of India constituted under section 3 of the Company Secretaries Act, 1980 and approved by the Central Government. The provisions contained in section 204 and section 205 shall not affect the duties and functions of the Board of Directors, chairperson of the company, managing director or whole-time director under this Act, or any other law for the time being in force.

4.14 Stock Exchange Board of India Initiatives

In September 2009 the SEBI Committee on Disclosure and Accounting Standards issued a discussion paper that considered proposals for:

a) Appointment of the chief financial officer (CFO) by the audit committee after assessing the qualifications, experience and background of the candidate;

b) Rotation of audit partners every five years;

c) Voluntary adoption of International Financial Reporting Standards (IFRS);

d) Interim disclosure of balance sheets (audited figures of major heads) on a half-yearly basis; and

e) Streamlining of timelines for submission of various financial statements by listed entities as required under the Listing Agreement.

136 Section 205 of the Companies Act, 2013.

137 Section 205 (2) of the Companies Act, 2013.

In early 2010, SEBI amended the Listing Agreement to add provisions related to the appointment of the CFO by the audit committee and other matters related to financial disclosures.\textsuperscript{139} However, other proposals such as rotation of audit partners were not included in the amendment of the Listing Agreement.\textsuperscript{140}

4.15 Ministry of Corporate Affairs Initiatives

Inspired by industry recommendations, including the influential CII recommendations, in late 2009 the MCA released a set of voluntary guidelines for corporate governance.\textsuperscript{141} The Voluntary Guidelines address a myriad of corporate governance matters including:

I. Independence of the boards of directors;
II. Responsibilities of the board, the audit committee, auditors, secretarial audits; and
III. Mechanisms to encourage and protect whistle blowing.\textsuperscript{142}

Important provisions include:

a) Issuance of a formal appointment letter to directors.

b) Separation of the office of chairman and the CEO.

c) Institution of a nomination committee for selection of directors.

d) Limiting the number of companies in which an individual can become a director.

e) Tenure and remuneration of directors.

f) Training of directors.

g) Performance evaluation of directors.

h) Additional provisions for statutory auditors.

In sum, the new Companies Act, 2013 is not only efficient and innovative but seeks to make the corporate management and governance in India fully

\textsuperscript{139} These measures have been introduced through an amendment to the Listing Agreement. See Securities and Exchange Board of India, Circular No. CIR/CFD/DIL/1/2010 (Apr. 5, 2010), available at www.sebi.gov.in/circulars/2010/cfddilcir01.pdf. (Visited on October 20, 2015).


\textsuperscript{141} For detailed evaluation of the substance of the voluntary guidelines and whether a voluntary approach is the correct approach, see Varottil, Rhetoric or Reality.

\textsuperscript{142} See MCA Voluntary Guidelines, 2009.
accountable, thereby, beneficial to all stakeholders and related professionals. Also, both broad categories of directors one having pecuniary relationship and others who are independent are naturally considered under the landmark Act. For number of matters, the Central Government has to prescribe by rules the limits for payment or procedure to be followed. Some stringent and minimum and maximum fines will be levied for contravention of these provisions. Punishment in the form of imprisonment of defaulting directors and Officers can also be awarded for such contravention of these provisions. Such provisions indicate that those in management are required to be vigilant about the compliance with provisions of the law and about Corporate Governance. It appears that in enacting such stringent provisions the Government has taken care of some of the deficiencies of the existing Act and tried to remove the same. Further, an attempt is made to address the issues which have arisen in some cases of corporate failures and Corporate Scams which have so far come to light. It is hoped that the Companies Act, 2013, if properly implemented and administered brings more discipline in the matter of Corporate Governance in the future.