

# POWERS, DUTIES & LIABILITIES OF BOARD OF DIRECTORS OF A COMPANY IN INDIA

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## POWERS

The directors' powers are normally set out in the articles. The shareholders cannot control the way in which the Board of Directors act provided its actions are within the powers given to the Board.

Section 291 of Companies Act, 1956 provides for general powers of the Board of directors. It mandates that the Board is entitled to exercise all such powers and do all such acts and things, subject to the provisions of the Companies Act, as the company is authorized to exercise and do. However, the Board shall not exercise any power and do any act or things which is required whether by the Act or by the memorandum or articles of the company or otherwise to be exercised or done by the company in general meeting.

Power of the individual directors – Unless the Act or the articles otherwise provide, the decisions of the Board are required to be the majority decisions only. Individual directors do not have any general powers. They shall have only such powers as are vested in them by the Memorandum and Articles.

Section 292(1) of the Companies Act, 1956 provides that the Board of directors of a company shall exercise the following powers on behalf of the company and it shall do so only by means of resolution passed at meeting of the Board:

- (a) the power to make calls on shareholders in respect of money unpaid on their shares;
- (aa) the power to authorize the buy-back referred to in the first proviso to clause (b) of sub-section (2) of section 77A;
- (b) the power to issue debentures;
- (c) the power to borrow moneys otherwise than on debentures;
- (d) the power to invest funds of the company; and
- (e) the power to make loan.

## DUTIES

### 1. Statutory Duties:

- (A) To file return of allotment: Section 75 of the Companies Act, 1956 requires a company to file with the Registrar, within a period of 30 days, a return of the allotments stating the specified particulars. Failure to file such return shall make the directors liable as 'officer in default'. A fine up to Rs. 5000/- per day till the default continues may be levied.
- (B) Not to issue irredeemable preference share or shares or share redeemable after 20 years: Section 80, as amended by Amendment Act, 1996, forbids a company to issue irredeemable preference shares or preference shares redeemable beyond 20 years. Directors making any such issue may be held liable as 'officer in default' and may be subject to fine up to Rs. 10,000/-.

- (C) To disclose interest (Section 299-300): In respect of contracts with director, Section 299 casts an obligation on a director to disclose the nature of his concern or interest (direct or indirect), if any, at a meeting of the Board of directors. The said Section provides that in case of a proposed contract or arrangement, the required disclosure shall be made at the meeting of the Board at which the question of entering into the contract or agreement is first taken into consideration. In the case of any other contract or arrangement, the disclosure shall be made at the first meeting of the Board held after the director become interested in the contract or arrangement. Every director who fails to comply with the aforesaid requirements as to disclosure of concern or interest shall be punishable with fine, which may extend to Rs. 50,000/-.
- (D) To disclose receipt from transfer of property (sec. 319): Any money received by the directors from the transferee in connection with the transfer of the company's property or undertaking must be disclosed to the members of the company and approved by the company in general meeting. Otherwise, the amount shall be held by the directors in trust for the company. This money may be in the nature of compensation for loss of office but in essence may be on account of transfer of control of the company. But if it is bona fide payment of damages for the breach of contract, then it is protected by sec. 321(3). Even no director other than the managing director or whole time director can receive any such payment from the company itself.
- (E) To disclose receipt of compensation from transferee of shares (Sec.320): If the loss of office results from the transfer (under certain conditions) of all or any of the shares of the company, its directors would not receive any compensation from the transferee unless the same has been approved by the company in general meeting before the transfer takes place. If the approval is not sought or the proposal is not approved, any money received by the directors shall be held in trust for the shareholders, who have sold their shares. Any such director, who fails to take reasonable steps as aforesaid, shall be punishable with fine, which may extend up to Rs. 2500/-.
- (F) Duty to attend Board meetings: A number of powers of the company are exercised by the Board of directors in their meetings held from time to time. Although a director may not be able to attend all the meetings but if he fails to attend three consecutive meetings or all meetings for a period of three months whichever is longer, without permission of the Board, his office shall automatically fall vacant [Section 283(1)(g)].
- (G) To convene statutory, Annual General meeting (AGM) and also extraordinary general meetings [ Section 165,166 &169]
- (H) To prepare and place at the AGM along with the balance sheet and profit & loss account a report on the company's affairs including the report of the Board of Directors (Section 173, 210 & 217).
- (I) To authenticate and approve annual financial statement (Section 215).
- (J) To appoint first auditor of the company (Section 224).
- (K) To appoint cost auditor of the company (Section 233B).
- (L) To make a declaration of solvency in the case of Members' voluntary winding up (Section 488).

## 2. General Duties:

- (A) Duty of good faith: The directors must act in the best interest of the company. Interest of the company implies the interest of the present and future members of the company on the footing that company would be continued as going concern.
- (B) Duty of care: A director must display care in performance of work assigned to him. He is, however, not expected to display an extraordinary care but that much care which a man of ordinary prudence would take in his own case. Any provision in the company's Articles or in any agreement that excludes the liability of the directors for negligence, default, misfeasance, breach of duty or breach of trust, is void. The company cannot even indemnify the directors against such liability.
- (C) Duty not to delegate: Director being an agent is bound by the maxim 'delegatus non potest delegare' which means a delegatee can not further delegate. Thus, a director must perform his functions personally. However, he may delegate his in certain conditions.

# LIABILITES

## 1. Liability to the company:

- (A) Breach of fiduciary duty: where a director acts dishonestly to the interest of the company, he will be held liable for breach of fiduciary duty. Most of the powers of directors are 'powers in trust' and therefore, should be exercised in the interest of the company and not in the interest of the directors or any section of members.
- (B) Ultra vires acts: Directors are supposed to act within the parameters of the provisions of the Companies Act, Memorandum and Articles of Association, since these lay down the limits to the activities of the company and consequently to the powers of the Board of directors. Further, the powers of the directors may be limited in terms of specific restrictions contained in the Articles of Association. The directors shall be held personally liable for acts beyond the aforesaid limits, being ultra vires the company or the directors.
- (C) Negligence: As long as the directors act within their powers with reasonable skill and care as expected of them as prudent businessman, they discharge their duties to the company. But where they fail to exercise reasonable care, skill and diligence, they shall be deemed to have acted negligently in discharge of their duties and consequently shall be liable for any loss or damage resulting therefrom.
- (D) Mala fide acts: Directors are the trustee for the moneys and property of the company handled by them, as well as exercise of the powers vested in them. If they dishonestly or in a mala fide manner, exercise their powers and perform their duties, they will be liable for breach of trust and may be required to make good the loss or damage suffered by the company by reason of such mala fide acts. They are also accountable to the company for any secret profits they might have made in course of performance of duties on behalf of the company. Directors can also be held liable for their acts of 'misfeasance' i.e., misconduct or willful misuse of powers.

**Liability to third parties:****Liability under the Companies Act:**

(A) Prospectus: Failure to state any particulars as per the requirement of the section 56 and Schedule II of the act or mis-statement of facts in prospectus renders a director personally liable for damages to the third party. Section 62 provides that a director shall be liable to pay compensation to every person who subscribes for any shares or debentures on the faith of the prospectus for any loss or damage he may have sustained by reason of any untrue or misleading statement included therein.

(B) With regard to allotment: Directors may also incur personal liability for:

(a) Irregular allotment, i.e., allotment before minimum subscription is received (Section 69), or without filing a copy of the statement in lieu of prospectus (Section 70) - [Section 71(3)] - Under section 71(3), if any director of a company knowing contravenes or willfully authorizes or permits the contravention of any of the provisions of section 69 or 70 with respect to all allotment, he shall be liable to compensate the company and the allottee respectively for any loss, damages or costs which the company or the allottee may have sustained or incurred thereby.

(b) For failure to repay application monies in case of minimum subscription having not been received within 120 days of the opening of the issue: Under section 69(5) read with SEBI guidelines, in case moneys are not repaid within 130 days from the date of the issue of the prospectus, the directors of the company shall be jointly and severally liable to repay that money with interest at the rate of 6 % per annum on the expiry of 130th day. However, a director shall not be liable if he proves that the default in repayment of money was not due to any misconduct or negligence on his part.

(c) Failure to repay application monies when application for listing of securities are not made or is refused: Under section 73(2) – where the permission for listing of the shares of the company has not been applied or such permission having been applied for, has not been granted, the company shall forthwith repay without interest all monies received from the applicants in pursuance of the prospectus, and, if any such money is not repaid within eight days after the company becomes liable to repay, the company and every director of the company who is an officer in default shall, on and from the expiry of the eighth day, be jointly and severely liable to repay that money with interest at such rate, not less than four per cent and not more than fifteen per cent, as may be prescribed, having regard to the length of the period of delay in making the repayment of such money.

(C) Unlimited liability: Directors will also be held personally liable to the third parties where their liability is made unlimited in pursuance of section 322(i.e., vide Memorandum) or section 323(i.e., vide alterations of Memorandum by passing special resolution). By virtue of section 322, the Memorandum of a company may make the liability of any or all directors, or manager unlimited. In that case, the directors, manager and the member who proposes a person for appointment as director or manager must add to the proposal for appointment as a statement that the liability of the person holding the office will be unlimited. Notice in writing to the effect that the liability of the person will be unlimited must be given to him by the following or one of the following person, namely: the promoters, the directors, manager and officers of the company before he accept the appointment.

Further, in case of limited liability Company, the company may, if authorized by the articles, by passing resolution alter its Memorandum so as to render the liability of its directors or of any director or manager unlimited. But the alteration making the liability of director or directors or manager unlimited will be effective only if the concerned officer consents to his liability being made unlimited. This alteration also, unless specifically consented to by any or all directors will not have any effect until expiry of the current term of office.

- (D) Fraudulent trading: Directors may also be made personally liable for the debts or liabilities of a company by an order of the court under section 542. Such an order shall be made by the court where the directors have been found guilty of fraudulent trading. Section 542(1), in this regard, provides that 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 creditors of the company or any other person, or for any fraudulent purpose, the court, on the application of the Official Liquidator, or the liquidator or any creditor or contributory of the company may if it thinks it proper so to do, declare that any persons who were knowingly parties to the carrying on 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 court may direct.

Further, section 542(3) provides that every person who was knowingly a party to the carrying on of the business in the manner aforesaid, shall be punishable with imprisonment for a term which may extend to two years, or with fine which may extend to fifty thousand rupees, or with both.

#### **Liability for breach of warranty:**

Directors are supposed to function within the scope of their authority. Thus, where they transact any business in respect of matters, ultra vires the company or ultra vires the articles, they may be proceeded against personally for any loss sustained by any third party.

#### **2. Liability for breach of statutory duties:**

The Companies Act, 1956 imposes numerous statutory duties on the directors under various sections of the Act. Default in compliance of these duties attract penal consequences. The various statutory penalties which directors may incur by reason of non-compliance with the requirements of Companies Act are referred to in their appropriate places.

#### **3. Liability for acts of co-directors:**

A director is the agent of the company except for matters to be dealt with by the company in general meeting and not of the other members of the Board. Accordingly, nothing done by the Board can impose liability on a director who did not participate in the Board's action or did not know about it. To incur liability he must either be a party to the wrongful act or later consent to it. Thus, the absence of a director from meeting of the Board does not make him liable for the fraudulent act of a co-director on the ground that he ought to have discovered the fraud.

#### **4. Criminal liability:**

Apart from the civil liability under that Act or under the common law, directors of a company may also incur criminal liability. Some of the provisions of the Companies Act, which make directors criminally liable, are as follows:

- (i) Section 44(4) – filing of prospectus or statement in lieu of prospectus containing untrue statement. Penalty – Two years imprisonment or / and fine up to Rs. 50000.
- (ii) Section 58A(5) – failure to repay deposits within the prescribed time limit as specified under sub sections (3) and (4) of section 58A. Penalty – Up to five years imprisonment and fine.
- (iii) Section 58A(6) - Accepting deposits or inviting deposits in excess of the prescribed limits. Penalty – up to five years imprisonment and fine.
- (iv) Section 63 - Issuing a prospectus containing untrue statement. Penalty – Imprisonment upto two years or/ and fine upto Rs. 50000.
- (v) Section 68 - Knowingly making a false, deceptive or misleading statement and there by inducing persons to invest money. Penalty – Imprisonment upto five years or/ and fine upto Rs. 1,00,000.
- (vi) Section 73 – Failure to repay excess application money. Penalty – Default in repayment of application money and interest is punishable with fine upto Rs. 50000 but if repayment is not made within six months from the expiry of eight day, also with imprisonment for a term upto one year.
- (vii) Section 84(3) – Fraudulently renewing a share certificate or issuing a duplicate share certificate. Penalty – Imprisonment upto six months or/ and fine upto Rs.1,00, 000.
- (viii) Section 105 – Concealing name of creditor or misrepresenting the nature and the amount of the debt or claim of any creditor. Penalty – Imprisonment upto one year or/ and fine or both.
- (ix) Section 202(1) – Undischarged insolvent acting as director. Penalty – Imprisonment upto two years or/ and fine upto Rs. 50000.
- (x) Section 207 – Default in distributing dividends. Penalty – Simple imprisonment upto three years and fine up to Rs. 1000 for every day during which the default continues.
- (xi) Section 209A – Failure to assist Registrar or any officer so authorized by Central Government in inspection of books of account, etc., of the company. Penalty – Imprisonment for a term not exceeding one year and fine to be not less than Rs. 50000.
- (xii) Section 210(5) – Failure to lay balance sheet, profit & loss account, etc., at the annual general meeting. Penalty – Imprisonment upto six months or/ and fine upto Rs. 10000.
- (xiii) Section 211(8) – Failure to comply with section 211 regarding form of balance sheet and matters to be stated therein and the content and disclosures to be made in the profit and loss account. Penalty – imprisonment upto six months or/ and fine upto Rs. 10000.

- (xiv) Section 217(5) – Failure to attach to balance sheet a report of the Board of directors. Penalty – Imprisonment upto six months or / and fine upto Rs. 20000.
- (xv) Section 221(4) – Failure to supply information to auditors. Penalty – Imprisonment upto six months or / and fine upto Rs. 50000.
- (xvi) Section 233B(11) – Audit of cost account of the company -Default in complying with the requirements of the section. Penalty – Imprisonment for a term that may extent to three years or with fine which may go upto Rs. 50000 or with both.
- (xvii) Section 250(9) – Failure to honour restrictions upon shares and debentures imposed by the CLB. Penalty – Imprisonment upto six months or / and fine upto Rs. 50000.
- (xviii) Section 293A(5) – Contribution to political party or for political purpose in contravention of section 293A. Penalty – Imprisonment upto three years and fine.
- (xix) Section 295(4) – Grant of loan to directors without obtaining previous approval of the Central Government. Penalty – Simple imprisonment upto six months or fine upto Rs. 50000.
- (xx) Section 299(4) – Failure to disclose interest in a contract or arrangement. Penalty – Fine which may extend to Rs. 50000.
- (xxi) Section 308(3) – Failure to disclose shareholdings. Penalty – Imprisonment upto two years or / and fine upto Rs. 50000.
- (xxii) Section 371 – Giving loans to other bodies corporate in excess of the limit prescribed under section 370. Penalty – Fine upto Rs. 50000 or simple imprisonment upto six months.
- (xxiii) Section 407 – Any person, whose agreement has been terminated or set aside under section 402, knowingly acts as a managing or other director before expiry of a period of five years from the date of termination, without approval of the CLB, attracts criminal liability. Penalty – Imprisonment upto one year or / fine upto Rs. 50000 [Section 407(2)].
- (xxiv) Section 488(3) – False declaration of company's solvency. Penalty – Imprisonment upto six months or / and fine up to Rs. 50000.
- (xxv) Section 209(8) – Non-compliance with the requirement of maintenance of proper books of account. Penalty – fine not less than Rs. 50000 and also with imprisonment not exceeding one year for each offence committed.