

Directors : Duties and Responsibilities

Seminar on Important Provisions of the Companies Act, 2013

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Director

- ▶ *DIRECTOR*” means a director appointed to the Board of a Company. [Section 2(34)].
- ▶ “*BOARD OF DIRECTORS*” or “*BOARD*”, in relation to a company, means the collective body of the directors of the Company.
[Section 2(1)(10)].

Role of a Director

- As an agent : Directors act as representatives of shareholders who execute decision making.
- Directors as employees : Director appointed as whole time employee.
- Directors as officers : Directors are treated as officers of an company.
- Directors as trustees : Director is trusted as trustee of company, money and property and powers entrusted to and vested in trustee only.

Positions held by Director

- Managing Director
- Manager
- Whole Time Director
- Key Managerial Personnel
- Officer in default
- Independent Directors

Managing Director – Section 2(54)

- ▶ “MANAGING DIRECTOR” - Director by virtue of Articles/Agreement/Shareholders’ Resolution.
- ▶ Entrusted with the substantial powers of Management of the Company.
- ▶ Includes a director occupying the position of Managing Director, by whatever name called.

Manager – Section 2(53)

- ▶ “MANAGER” - An individual who, subject to the superintendence, control and direction of the Board of Directors.
- ▶ Has the Management of the whole, or substantially the whole, of the affairs of a Company.
- ▶ Includes a director occupying the position of Manager, by whatever name called.

Whole Time Director – Section 2(94)

- ▶ “WHOLE TIME DIRECTOR” includes a director in the whole-time employment of the Company.

Officer who is in Default– Section 2(60)

“OFFICER WHO IS IN DEFAULT” includes a director in the following instances:

- Whole time Director.
- Key Managerial Personnel (KMP).
- In case of no KMP such director as specified by the Board and who has consented as such.
- If no Director is so specified all the Directors
- Person with whose advice Board of Directors is accustomed to act, other than a person who gives in a professional capacity.

Independent Director (“ID”)

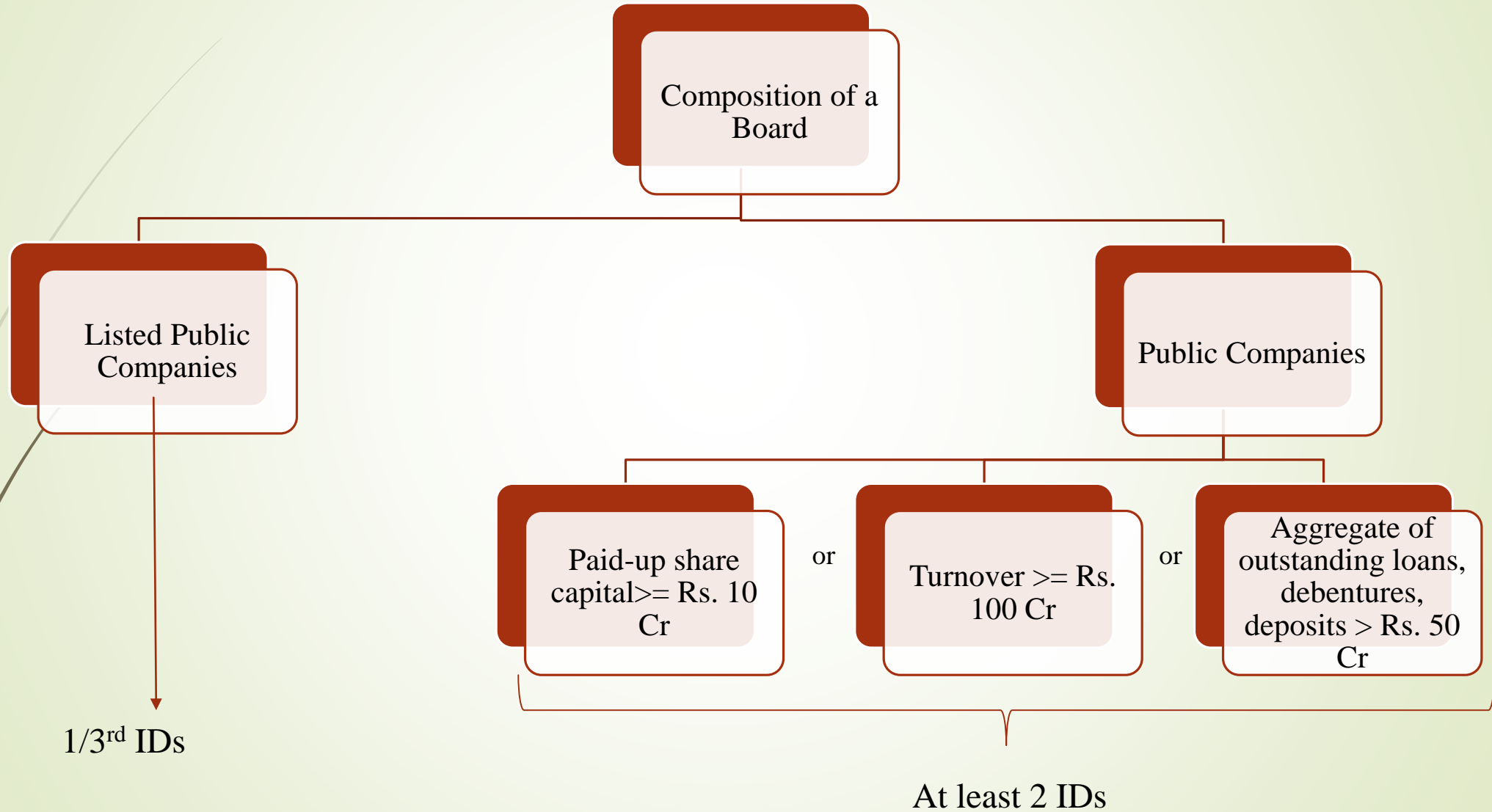
– Section 2(47) r.w.s 149(5)

- Separate Definition of IDs under the Companies Act.
- Listed Public Company to have at least 1/3rd of the total number of directors as independent directors.
- No. of Independent Director for unlisted Company and its subsidiaries will be prescribed by Central Government.
- Limited Liability of Independent Directors – Liability only for 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.

ID

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Sec 149(4) r.w. Companies (Appointment and Qualification) Rules, 2014



Qualifications of an ID

Section 149(6)

- Other than MD or WTD or Nominee Director.
- In the opinion of the Board, a person of integrity, possessing relevant expertise and experience.
- Not a promoter of the company or its holding, subsidiary or associate company.
- Not related to promoters of the company or its holding, subsidiary or associate company.
- No pecuniary relationship with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year.

- Relatives not to have pecuniary relationship or transaction with the company, its holding, subsidiary or associate company, or their promoters, or directors
 - Threshold- two per cent or more of its gross turnover or total income or fifty lakh rupees, whichever is lower during the two immediately preceding financial years or during the current financial year.
- Neither himself nor his relatives
 - ❑ is or was KMP/employee of the company or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed is or has been employee or proprietor or a partner, in such three financial years, of—
 - a firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary or associate company; or

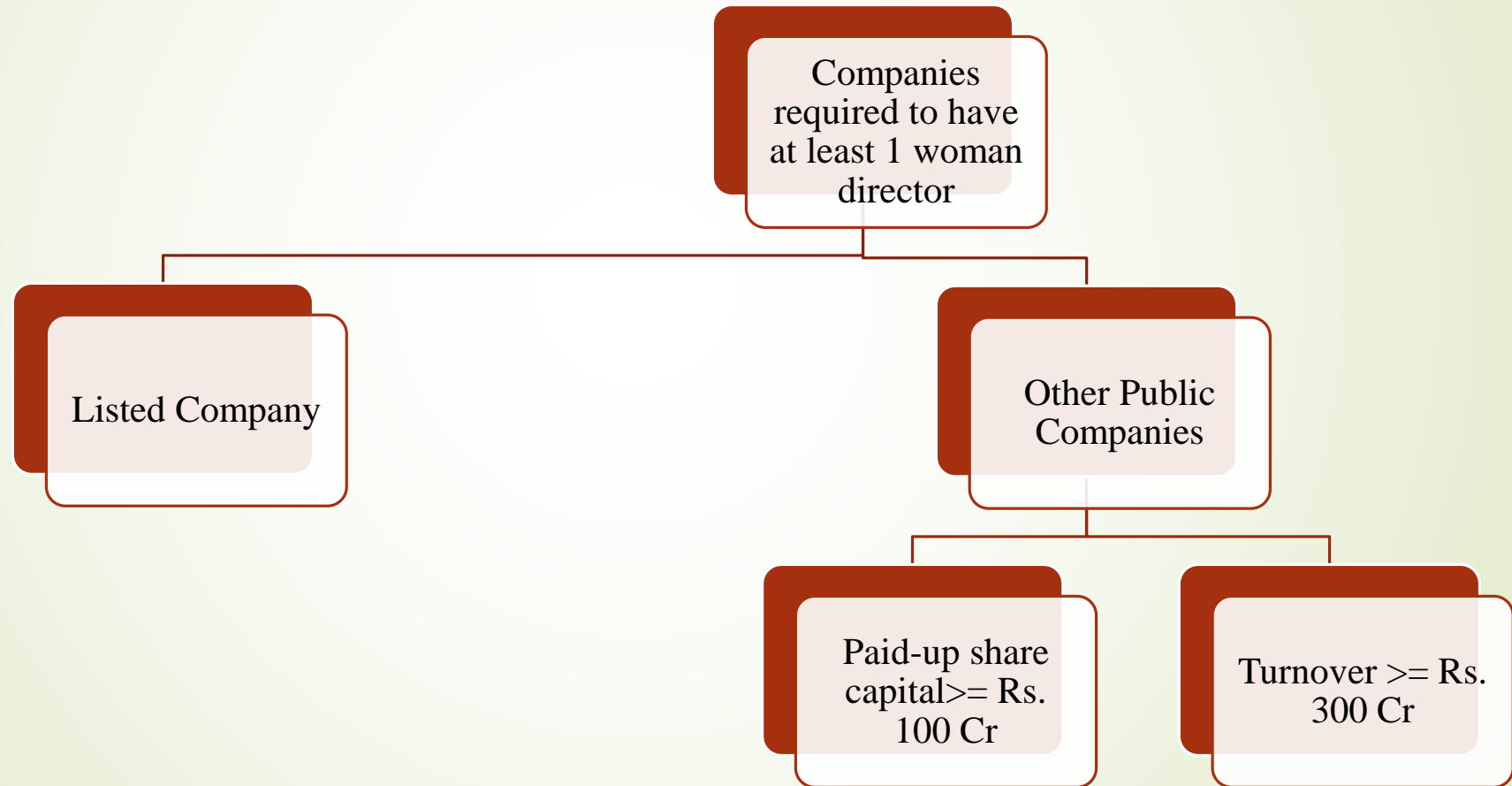
- ❑ any legal or a consulting firm that has or had any transaction with the company, its holding, subsidiary or associate company amounting to *ten per cent or more of the gross turnover* of such firm.
 - ❑ holds with his relatives *two per cent or more of the total voting power* of the company.
 - ❑ is a CEO or a director of any non-profit organisation that receives *twenty-five per cent* or more of its receipts from the company, its promoters, directors or its holding, subsidiary or associate company or that holds *two per cent or more of the total voting power* of the Company.
- *Companies (Appointment and Qualification) Rules, 2014* - IDs to possess appropriate skills, experience and knowledge in finance, law, sales, marketing etc.

Pecuniary Relationship - Meaning

- Dictionary Meaning of ‘pecuniary’ – Oxford definition - *“something to do with money”*.
- General Circular 14/2014– IDs entering into transactions with the company that are at par with the members of general public and at the same price will not be said to have ‘pecuniary relationship’. Also, receipt of fee, reimbursement of expenses and profit related commission to be excluded from “pecuniary relationship.”

Woman Director

Second Proviso to sec149(1) and *Companies (Appointment and Qualification) Rules, 2014*



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NO SPECIFIC REQUIREMENT OF WOMAN DIRECTOR TO BE INDEPENDENT

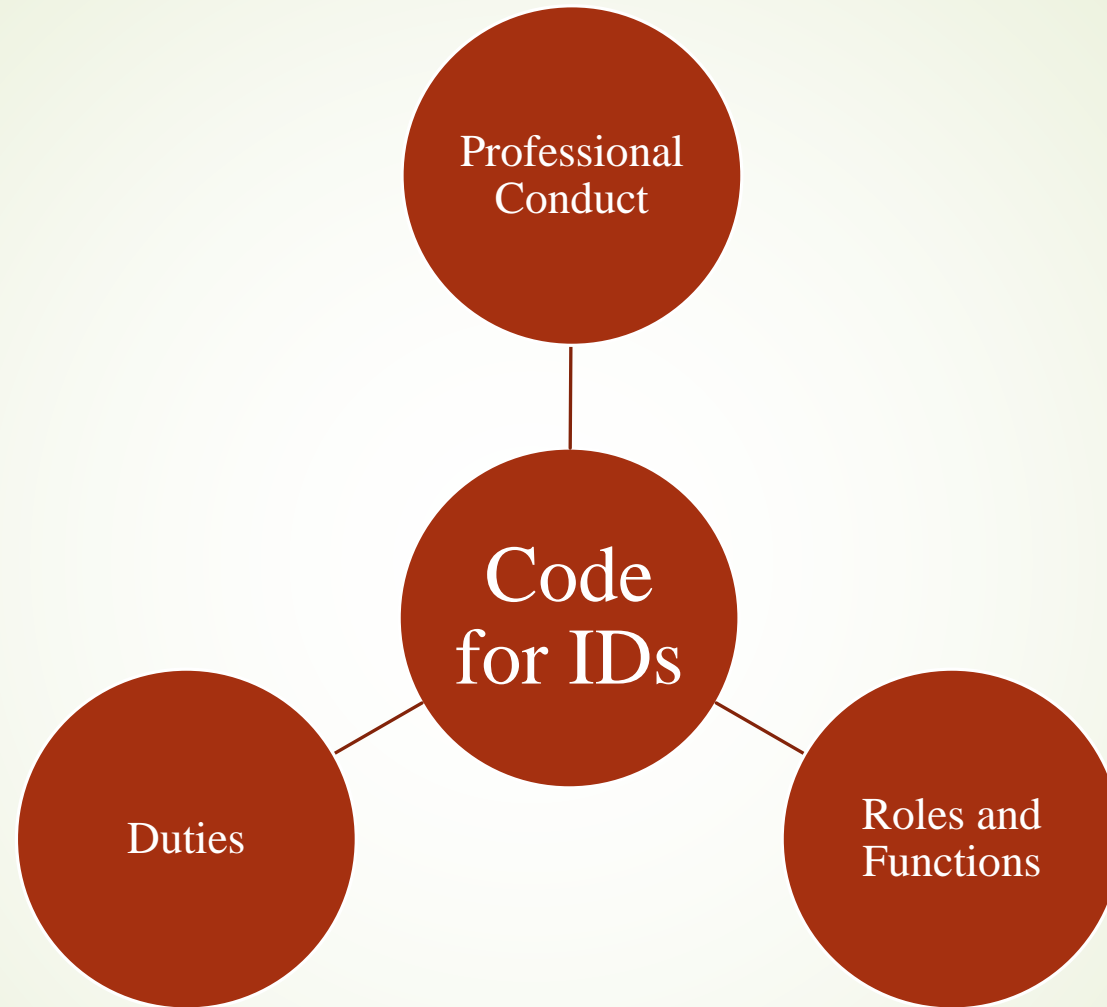
Separate Meeting of IDs

Schedule IV

- IDs to hold atleast 1 meeting without attendance of non-independent directors
- In such meeting, IDs to:
 - ❑ Review performance of non-independent directors, Board and the Chairperson of the Company.
 - ❑ Assess the data flow between the Board and Management that is required for the Board to effectively perform their functions.

Schedule IV

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I. Professional conduct

- To act objectively and constructively while exercising duties.
- To exercise responsibilities in *bona fide* manner.
- Refrain from abusing position to the detriment of the company or its shareholders.
- To inform the Board on loss of independence.
- To assist in implementing the best corporate governance practices.

II. Roles and Functions

- Bring an independent judgment on the Board's deliberations on issues of strategy, performance, risk management, resources, key appointments and standards of conduct.
- Objectively evaluate Board and management performance.
- Satisfy on integrity of financial information, financial controls and the systems of risk management.
- Safeguard interests of all stakeholders, especially minority shareholders.
- Determine appropriate levels of remuneration of executive directors, KMPs and senior management, have a prime role in their appointment and recommend their removal, where necessary.
- Arbitration in the interest of the company in case of conflict between management and shareholder's interest, etc.

III. Duties

- Regularly update and refresh skills, knowledge and familiarity with the company .
- Seek appropriate clarification or amplification of information.
- Seek professional advice and expert opinion at the expense of the company wherever necessary.
- Strive to attend all meetings of the Board, Committees and shareholders
- Be well informed about the company and the external environment in which it operates.
- Maintain confidentiality of information, including commercial secrets, technologies, advertising and sales promotion plans, unpublished price sensitive information, unless such disclosure is expressly approved by the Board or required by law. Ensure that-
 - ❑ adequate deliberations are held before approving **related party transactions**.
 - ❑ company has an adequate and functional **vigil mechanism**.

Other provisions

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- *Sec 149(9)* - IDs not eligible for Stock Options.
- *Sec 149 (12)* - IDs to be responsible only for any omission or commission committed with their knowledge or consent or connivance or where they have acted without diligence.

Overview of provisions of the Act and Listing Regulations

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| Particulars | The Act | Listing Regulations |
|-------------------------------|--|--|
| Composition of Board | <ul style="list-style-type: none"> Listed company – 1/3rd to be IDs Other prescribed public companies – minimum 2 IDs | <ul style="list-style-type: none"> If chairman is non-executive director – 1/3rd directors to be independent If chairman is executive or non-executive but related to promoter - 1/2 directors to be independent |
| Requirement of Woman Director | <ul style="list-style-type: none"> Listed companies and other prescribed companies to have minimum 1 woman director | <ul style="list-style-type: none"> All listed companies to have minimum 1 woman director |
| Qualifications of IDs | <ul style="list-style-type: none"> Not an MD/WTD/nominee director Possess integrity, skills, knowledge No pecuniary relationship with the company-remuneration excluded from pecuniary relationship Not a KMP/employee Not a part of auditing firm, legal consulting firm Does not hold directly or through relatives \geq 2% of the voting power Other conditions | <ul style="list-style-type: none"> ID not to have material pecuniary relationship except for receiving remuneration ID not to be the material supplier service provider or customer or a lessor or lessee of the company ID not to be less than 21 years of age. Other conditions similar to the 2013 Act. |

| Particulars | The 2013 Act | Listing Regulations |
|---------------------------------|--|---|
| Appointment and Tenure | <ul style="list-style-type: none"> • Approval at shareholders' meeting • Communication through letter of appointment • 2 consecutive terms of 5 years each • Breathing period of 3 years before reappointment after 2 terms • Tenure of 5 years to be considered from the commencement of the Act. • But fresh appointment to be made under the 2013 Act within one year from April 1, 2014. | <ul style="list-style-type: none"> • Similar provisions |
| Limit on number of directorship | <ul style="list-style-type: none"> • Total Directorship limit – 20 • Directorship in public companies - 10 | <ul style="list-style-type: none"> • Basic Limit (as independent director) – 7 • Limit if individual is serving as a WTD - 3 |
| Separate Meeting of IDs | <ul style="list-style-type: none"> • IDs to hold atleast 1 meeting without attendance of non-independent directors | Similar Provisions |

Statutory Liabilities of Directors

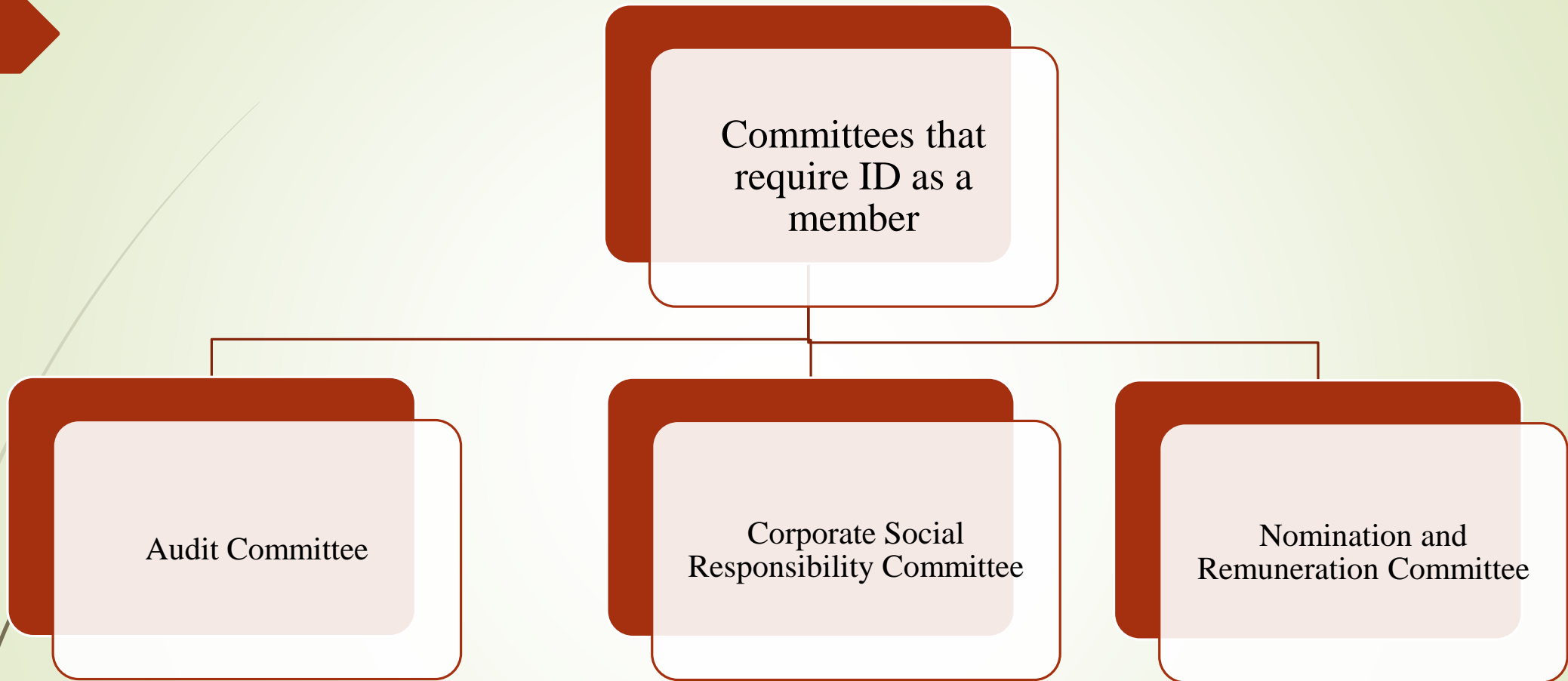
- For misstatements in prospectus (sections 34 & 35)
- For breach of solvency declaration (section 68)
- For breach of directors' duties (section 166)
- For fraudulent trading (section 339)
- For offences where no specific punishment is prescribed (section 450)
- Intimation of resignation as director to be provided to ROC (section 168)

Disclosure of Interest by a Director – (Section 184)

- Every Director shall disclose his interest in a third party before the company enters into a contract with such third party.
- Every director shall at the first meeting of the Board where it participates as a director and thereafter, at the first meeting of every financial year disclose his concern or interest in any company, body corporate, firm or association of individuals
- Such information is required to be provided in a declaration in Form MBP-I

Restrictions on Directors

- Prohibition of Insider Trading – Section 195
- Restriction on acquisition on assets from the company and vice versa by way of cash – section 192
- Prohibition on Forward dealing in securities.



Audit Committee

(Sec 177)

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| Particulars | The 2013 Act | Listing Regulations |
|--------------------|---|--|
| <i>Composition</i> | <ul style="list-style-type: none">• Committee to consist of minimum 3 directors• IDs to form majority. | <ul style="list-style-type: none">• Committee to consist of minimum 3 directors• 2/3rd members to be independent• Chairman to be independent |
| <i>Functions</i> | <ul style="list-style-type: none">• Recommendation for appointment and Remuneration of Auditors• Examination of financial statement an Auditors' report• Approval of Related party transactions• Evaluation of internal financial controls and risk management systems• Monitoring end use of funds raised through public issue | <p>Functions in addition to those mentioned in the Act</p> <ul style="list-style-type: none">• Reviewing the adequacy of internal audit function• Looking into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of non-payment of declared dividends) and creditors• Approval of appointment of CFO |

Nomination and Remuneration Committee (Sec 178)

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| Particulars | The Act | Listing Regulations |
|--------------------|---|--|
| <i>Composition</i> | <ul style="list-style-type: none"> • Committee to consist minimum 3 non-executive directors • IDs to form majority | <ul style="list-style-type: none"> • Committee to consist minimum 3 non-executive directors • IDs to form majority • Chairman to be independent |
| <i>Functions</i> | <ul style="list-style-type: none"> • Appointment & Removal of Directors • Evaluation of Directors performance • Formulate criteria for qualification and independence of directors • Recommend remuneration policy for directors, KMPs, key employees | Functions similar to those mentioned under the Act |

Corporate Social Responsibility(“CSR”) Committee

(Sec 135)

| Particulars | The Act | Listing Regulations |
|--------------------|---|---|
| <i>Composition</i> | <ul style="list-style-type: none"> • Committee to consist of minimum 3 directors • Of this minimum 1 must be ID | No requirement under the LA to form the committee |
| <i>Functions</i> | <ul style="list-style-type: none"> • Formulate and recommend CSR Policy to the Board in line with Schedule VII • Recommend expenditure to be incurred on CSR activities • Monitor CSR policy | |

Risk Management (“RM”) Committee

| Particulars | The Act | Listing Regulations |
|--------------------|--|---|
| <i>Composition</i> | <ul style="list-style-type: none"> No requirement under the Act to form such a Committee. | <ul style="list-style-type: none"> The majority of members of Risk Management Committee shall consist of members of the board of directors. The Chairperson of the Risk management committee shall be a member of the board of directors and senior executives of the listed entity may be members of the committee. |
| <i>Functions</i> | | <ul style="list-style-type: none"> The board of directors shall define the role and responsibility of the Risk Management Committee and may delegate monitoring and reviewing of the risk management plan to the committee and such other functions as it may deem fit. The provisions of this regulation shall be applicable to top 100 listed entities, determined on the basis of market capitalisation, as at the end of the immediate previous financial year. |

Obligations of IDs under the Listing Regulations

- IDs in the meeting shall, *inter alia* :
 - review the performance of non-independent directors and board of directors.
 - review the performance of the chairperson of the listed entity.
 - assess the quality, quantity and timeliness of flow of information between the management of the listed entity and the board of directors.
- Reviewing and guiding corporate strategy, major plans of action, annual budgets and business plans, setting performance objectives, monitoring implementation and corporate performance, and overseeing major capital expenditures, acquisitions and divestments.
- Selecting, compensating, monitoring and, when necessary, replacing key managerial personnel and overseeing succession planning.

Responsibilities of the Board of Directors under the Listing Regulations

- Ensuring a transparent nomination process to the board of directors.
- Monitoring and managing potential conflicts of interest of management, members of the board of directors and shareholders, including misuse of corporate assets and abuse in related party transactions.
- Ensuring the integrity of the listed entity's accounting and financial reporting systems, including the independent audit, and that appropriate systems of control are in place, in particular, systems for risk management, financial and operational control, and compliance with the law and relevant standards.
- Overseeing the process of disclosure and communications.
- Monitoring and reviewing board of director's evaluation framework.

Contd.

- The Board of Directors shall set a corporate culture and the values.
- Members of the board of directors shall act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the listed entity and the shareholders.
- The board of directors shall maintain high ethical standards and shall take into account the interests of stakeholders.
- The board of directors shall consider assigning a sufficient number of nonexecutive members of the board of directors capable of exercising independent judgement to tasks where there is a potential for conflict of interest.
- In order to fulfil their responsibilities, members of the board of directors shall have access to accurate, relevant and timely information.

Conclusion

- ▶ The new law assumes directors and key management personnel to be the sentinels of governance.
- ▶ The attribution of criminality to the "officer who is in default" is established under section 2(60) of the Companies Act, 2013. He shall be liable to penalty or imprisonment.
- ▶ Due to the excess liability on independent directors today, they are forced to serve more as advisors to the controlling shareholder rather than protectors of interest of the minority shareholder.

THANK YOU

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