

# Duties and Liabilities of Directors under India's Companies Act, 2013

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## Abstract

This paper examines the duties and liabilities of directors under the Companies Act, 2013, with particular emphasis on their statutory recognition and practical enforcement within India's corporate governance framework. It analyzes the codification of fiduciary duties under Section 166 and explores the scope of civil and criminal liabilities arising from breaches, including fraud, negligence and misstatements in corporate disclosures. The study also evaluated the concept of "officer in default", which extends accountability to individuals responsible corporate misconduct. Further, the paper considers the legal protections available to directors, such as the business judgment rule and safeguards for independent directors under Section 149(12), highlighting the balance between accountability and commercial decision making. It also addresses emerging challenges in areas like ESG obligations, digital governance and increased regulatory scrutiny, which have expanded the scope of directors' responsibilities. The paper concludes that while the Act has strengthened corporate governance, greater clarity and consistencies in enforcement are essential to ensure fairness and effectiveness.

**Keywords:** Directors' duties, Corporate Governance, Civil Liability, Criminal Liability, Fiduciary Duties

## Introduction

Corporate governance in India has evolved significantly over the past few decades in response to the economic reforms, regulatory developments and major corporate scandals at the heart of this governance structure are company directors, who are entrusted with responsibility of steering corporate strategy, supervising management and safeguarding the interests of the shareholders and other stakeholders. In a corporate environment often characterized by promoter-dominated ownership patterns, directors play a particularly crucial role in ensuring transparency, accountability and ethical decision making.

The transformation of corporate regulation in India gained momentum after the economic liberalization of 1990's. financial scandals such as the Harshad Mehta scam exposed serious weakness in regulatory oversight and corporate governance mechanisms. In response, the Securities exchange Board of India introduced governance reforms inspired by global developments such as the Cadbury Committee Report in United Kingdom. However it was the corporate fraud at Satyam Computer Services in 2009 that truly underscored the urgent need for stronger board accountability and stricter statutory duties.

While the Companies Act, 1956 laid down the basic framework of fiduciary obligations, it lacked clarity, effective enforcement mechanism and sufficient safeguards for independent oversight. The gap was addressed through the enactment of the Companies Act, 2013, which marked a watershed moment in Indian corporate law. The 2013 Act codified director's duties under Section 166, mandated the

appointment of independent directors under Section 149 and introduced the penalties under Section 447. These reforms were designed to align India's corporate governance standards with international best practices and enhance investor confidence.

Despite these progressive changes, significant challenges remain. Ambiguity persists regarding the extent of director's liability, particularly in cases involving negligence, oversight failures, or the role of independent directors under Section 149(12). Divergent interpretations by regulatory authorities and adjudicatory bodies such as SEBI and National Company Law Tribunal (NCLT) have led uncertainty in enforcement. This inconsistency not only complicates compliance but may also discourage competent professionals from accepting directorship position due to fear of disproportionate liability.

Against the backdrop, this paper seeks to examine the duties and liabilities of directors under the Companies Act, 2013 in a structured and critical manner. Specifically it aims to analyze the statutory duties and liabilities of directors under the act; to examine the scope of civil and criminal liabilities arising from breaches, including fraud and negligence; to evaluate the effectiveness of the legislative framework through statutory provisions and judicial precedents and to suggest measures that may promote clarity and consistency in enforcement.

The research adopts an analytical methodology. It relies primarily on the statutory provisions of the Companies Act, 2013, relevant SEBI regulations and leading judicial decisions, supplemented by scholarly commentary and secondary literature for interpretative analysis. The study does not employ empirical methods but focuses on the critical examination of the existing legal framework and practical implications of the existing legal framework.

### **Concept of Directors under the Companies Act, 2013**

Definition of "Director" (Section 2(34))

Section 2(34) of the Companies Act, 2013 defines a "director" as a person appointed to the Board of a company. The definition further clarifies that any individual occupying the position of director, by whatever name called, shall be treated as a director for the purposes of the Act<sup>1</sup>. This indicates that the law adopts a substance over-form approach, focusing not merely on formal designation but on the functional role performed within corporate governance.

The inclusive nature of this definition ensures that individuals who exercise real control over corporate affairs cannot evade liability merely because they are not formally designated as directors. Courts have often examined the actual role, authority, and participation of individuals in determining whether they fall within the ambit of the term director. Thus, the statutory definition strengthens accountability by preventing misuse of corporate structures to shield any de facto decision-makers.

### **Legal Position: Agent, Trustee, Officer**

The legal status of a director is unique and multifaceted. Though a company is a separate legal entity, it acts through human agency and directors constitute the primary decision-making body. Their legal character has traditionally been described under three interrelated capacities:

1. **Directors as Agents:** Directors act as agents of the company when entering into contracts or conducting transactions on its behalf. Since a company is an artificial legal person, it can operate

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<sup>1</sup> Unknown, U. (n.d.). Appointment and Qualifications of Directors. In *COMPANIES ACT, 2013*. <https://www.icsi.edu/media/portals/0/APPOINTMENT%20AND%20QUALIFICATIONS.pdf>

only through its Board. When directors act within the scope of their authority, their actions bind the company. However, if they exceed authority or act ultra vires, they may incur personal liability.

2. **Directors as Trustees:** although directors not act as trustees in the strict technical sense under trust law, directors are treated as trustees of the company's assets and powers. They are expected to act in good faith and for benefit of company as whole. This fiduciary dimension requires directors to avoid conflict of interest, misuse of corporate opportunities, and diversion of assets. Their fiduciary obligations are now codified under Section 166 of the Act, reinforcing principles that are earlier primarily under common law.
3. **Directors as Officers in Default:** Under Section 2(60) of the Act, directors may be categorized as "officers in default" and held liable for statutory non-compliance. This concept expands accountability by attaching liability not merely to the company but also to those individuals responsible for governance failures.<sup>2</sup> Thus, directors may face civil penalties, criminal sanctions or disqualification for breach of statutory duties.

Indian courts have often described directors as the "brain and nerve centre" of the company, emphasizing their role in shaping corporate conduct and ensuring regulatory compliance.

### Types of Directors under the Companies Act, 2013

The Companies Act, 2013 introduces a structures classification of directors to promote specialization, independence and diversity within corporate boards.

1. **Executive Directors:** they are involved in the day to day management of the company. These include positions such as Managing Director (MD) and Whole-time Director (WTD), appointed under Section 196 of the Act. They exercise substantial managerial powers pursuant to board resolutions or contractual agreements. Due to their active role in operations, executive directors often bear greater exposure to liability for operational misconduct and compliance failure.
2. **Non-Executive Directors:** they are not engaged in daily management functions. Instead they provide strategic guidance, policy oversight and independent supervision of executive management. Their role strengthens checks and balances within the corporate governance framework. They maybe promoters, shareholders or professional representatives.
3. **Independent Directors (Section 149):** independent directors represent one of the most significant reforms introduces by the Companies Act, 2013. Section 149 mandates the appointment of independent directors in listed companies and certain prescribed classes of public companies. At least one-third of the board of a listed company must consist of independent directors.

An independent director must not have any pecuniary relationship with the company, its promoters or its subsidiaries.<sup>3</sup> The objective is to ensure unbiased judgment and protect minority shareholder interests.

4. **Nominee Directors:** They are appointed by financial institutions, the government or other stakeholders pursuant to contractual agreements or statutory provisions. They represent the interests of their nominating authority but are nevertheless bound by fiduciary duties toward the company. They cannot prioritize the nominator's interests at the expense of the company's welfare.

<sup>2</sup> Asthana, S., & Asthana, S. (2023, December 18). *Directors in Company Law*. iPleaders. <https://blog.ipleaders.in/director-companies-act-2013/>

<sup>3</sup> Acharya, M. (2025, April 21). *Types of directors in a company*. Cleartax. <https://cleartax.in/s/types-of-directors-in-a-company>

5. **Woman Director:** to promote gender diversity and inclusive governance, the Act mandates the appointment of at least one director woman director in certain prescribed classes of companies, including listed entities and large public companies.
6. **Additional and Alternate Directors:** Section 161 provides for the appointment of Additional Directors and Alternate Directors.
  - Additional Directors may be appointed by the Board if authorized by the Articles of Association and hold office until the next Annual General Meeting (AGM).
  - Alternate Directors are appointed to act in place of a director who is absent from India for a period not less than 3 months. Their tenure is co-extensive with that of original director.

### Statutory Duties of Directors

Section 166 of the Companies Act, 2013 marks a significant development in Indian corporate law by expressly codifying the duties of directors. Before 2013, directors' obligations were largely drawn from English common law principles and judicial precedents. These standards, though well-established, were often broad and sometimes inconsistently applied. The need for clarity became especially evident after the corporate fraud at Satyam Computer Services, which exposed serious lapses in board oversight and accountability.

By incorporating directors' duties directly into the statute, Section 166 transformed what were once largely judge made fiduciary principles into clear, enforceable legal obligations.<sup>4</sup> These duties apply uniformly to all categories of directors and are personal in nature. A breach may attract civil liability, regulatory action, or in serious cases, criminal consequences under other provisions of the Act.

- **Duty to Act in Accordance with Article of Association (Section 166(1))**

The first statutory obligation requires directors to act in accordance with the company's Articles of Association (AoA). The AoA functions as the internal constitution of the company, outlining its governance framework, powers and procedures. Directors derive their authority from this document, and any action taken beyond its scope may be declared invalid.

This duty reinforces the principle that directors cannot exercise powers arbitrarily or beyond the authority granted to them by shareholders. The importance of adherence was highlighted in *Dale & Carrington Invt. (P) Ltd vs P.K. Prathapan* (2005), where the Supreme Court invalidated actions taken in excess of corporate authority.

- **Duty to Act in Good Faith (Section 166(2))**

Section 166(2) requires directors to act in good faith and in a manner they reasonably believe to be in the best interests of the company. Notably, the provision extends this consideration to various stakeholders, including employees, shareholders, the community and the environment. This gave a broader stakeholder-oriented model of governance.

Good faith involves honesty of intention, loyalty to the company, and the absence of improper motives. Directors must prioritize long-term corporate welfare over personal benefit or short-term gains. Courts generally evaluate whether decisions were made honestly and with genuine belief in the company's interest, rather than merely examining outcomes.

- **Duty to Exercise due and Reasonable Care, Skill and Diligence (Section 166(3))**

Section (166(4) introduces a standard of reasonable care, skill and diligence expected from directors. Th-

<sup>4</sup> *Section 166 of Companies Act, 2013: Duties of directors.* (2014, September 6). <https://ibclaw.in/section-166-of-the-companies-act-2013-duties-of-directors/>

is represents a move toward a more objective benchmark. Directors are expected to demonstrate the level of confidence and attention that a reasonably prudent person in a similar position would exercise. The duty requires active participation in broad deliberations, informed decision-making, and appropriate supervision of company affairs. Directors cannot remain passive or blindly rely on management representations. The importance of proactive oversight was emphasized in proceedings concerning Manpasand Beverages (2022), where directors were scrutinized for failing to detect financial irregularities despite access to relevant information.<sup>5</sup>

- **Duty Not to Achieve Undue Gain (Section 166(5))**

Section 166(5) further strengthens fiduciary accountability by prohibiting the directors from securing undue gain or gain advantage for themselves, their relatives or associates. If a director derives any improper benefit by the virtue of their position, they are obligated to repay the amount to the company. The provision codifies the long-standing equitable principle against secret profits. It serves as a deterrent against insider misuse of information, diversion of the corporate opportunities and other forms of self-enrichment at the expense of the company.

- **Duty Not to Assign Office (Section 166(6))**

Finally, Section 166(6) provides that a director cannot assign their office to another person. Any such assignment is void. The rationale behind this rule is that directorship is a position of personal trust and responsibility. Since duties are fiduciary and personal in nature, they cannot be transferred or delegated in entirety.

### **Fiduciary Duties and Corporate Governance Principles**

Fiduciary duties lie at the heart of corporate governance. They require directors to act with loyalty, honesty and due care while managing the affairs of the company. Although these duties originated in equitable and common law principles, they now have statutory recognition under Section 166 of the Companies Act, 2013.<sup>6</sup> Their codification became especially significant after corporate failures such as the fraud at Satyam Computer Services, which exposed weakness in broad oversight ethical accountability.

In India, where many companies operate under promoter-controlled structures, fiduciary duties help reduce conflicts of interest and protect minority shareholders. Fiduciary duties ensure that directors exercise their powers for the benefit of the company as a whole, rather than personal advantage.

### **Explanation of Fiduciary Relationship**

A fiduciary relationship is a relationship which is founded on trust and confidence. Directors occupy such a position in relation to the company. They are often described as agents, trustees and officers of the company. While not trustees in the strict technical sense, they are treated as trustees of corporate assets and powers.

The classical position was laid down in *Percival v. Wright* (1902), which held that directors owe their duties to the company and not to individual shareholders. Indian law follows this principle, though exceptions may arise in cases of oppression or special circumstances under Section 241 and 242 of the Act:

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<sup>5</sup> *Analyzing Directors' Duty of Care under the Companies Act, 2013*. (2023, March 30). IndiaCorpLaw. <https://indiacorplaw.in/2023/03/29/analyzing-directors-duty-of-care-under-the-companies-act-2013/>

<sup>6</sup> *Manupatra Academy*. (n.d.). <https://www.manupatraacademy.com/legalpost/fiduciart-duty-of-director-of-company>

- **Section 241** of the Companies Act, 2013 allows members (shareholders) to approach NCLT when a company's affairs are conducted in a manner that is oppressive, prejudicial or amounts to mismanagement.
- **Section 242** empowers the NCLT to pass appropriate orders to remedy such oppression or mismanagement and safeguard the interests of the company and its members.

Fiduciary framework requires directors to maintain confidentiality, avoid secret profits, refrain from exploiting corporate opportunities and safeguard company assets with utmost good faith (uberrima fides). Thus their role therefore goes beyond that of ordinary employees and places them in a position of stewardship.

### **Doctrine of Good Faith**

This doctrine of good faith is reflected in Section 166(2) which requires directors to act honestly and in what they reasonably believe to be the best interests of company. Notably, the provision also recognizes the interests of stakeholders such as employees, the community and the environment.

Good faith demands fairness, transparency and the absence of improper motives. Courts generally examine whether directors acted with honest intention and reasonable belief, rather than judging decisions only by their financial outcomes.

### **Proper Purpose Role**

The proper purpose rule requires directors to exercise their powers only for the purposes for which they were conferred. Even where directors possess legal authority, misuse of that authority, misuse of that authority for collateral objectives- such as altering control or disadvantaging minority shareholders- constitutes a breach of fiduciary duty.

In *Dale & Carrington Inv. (P) Ltd. v. P.K. Prathapan* (2005), the Supreme Court invalidated a share allotment designated to shift control within the company, emphasizing that powers must be exercised for legitimate corporate purposes. Basically, this rule acts as a safeguard against managerial abuse.

### **Corporate Social Responsibility (Section 135)**

Section 135 of the Companies Act, 2013 introduces Corporate Social Responsibility (CSR) obligations for companies meeting prescribed financial thresholds. Eligible companies must constitute a CSR Committee and spend a specified percentage of profits on approved social initiatives.<sup>7</sup>

While CSR extends beyond traditional fiduciary concepts, it reflects the evolving understanding of corporate governance in India. Directors are responsible for overseeing compliance and ensuring proper disclosure, thereby integrating social accountability into broad responsibilities.

### **Role of Independent Directors**

Independent Directors under Section 149(4) to Section 149(6) of the Companies Act, 2013 are the non-executives that lack material promoter ties or pecuniary relationships with the company. They fulfill fiduciary duties by delivering impartial scrutiny and countering any insider dominance in Indian companies.

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<sup>7</sup> Nexdigm. (n.d.). *Duties of Directors in India – Legal responsibilities & Governance guidelines* | Nexdigm. <https://www.nexdigm.com/doing-business-in-india/duties-of-directors.php>

## Civil Liabilities of Directors

Civil Liability under the Companies Act, 2013 attaches personal financial responsibility to directors for breaches of statutory or fiduciary duties. Unlike criminal liability, which is punitive in nature, civil liabilities are primarily compensatory and remedial. It seeks to restore the company or affected stakeholders to the position they would have occupied had the wrongful act not occurred. Such liability may arise in the form of damages, restitution, and disgorgement of profits or regulatory directions issued by the adjudicatory authorities. Civil liabilities of directors are:

- 1. Breach of Fiduciary Duty:** A breach of duties prescribed under Section 166- whether arising from lack of good faith, negligence or disloyal conduct- may render directors liable to compensate the company for losses suffered.<sup>8</sup> Courts may order payment of damages, recovery of secret profits or equitable remedies such as rescission of improperly executed contracts.  
The scope of oversight liability was illustrated in *Manpasand Beverages Ltd. V. SEBI (2022)*, where NCLT imposed Rs. 10 Lakh damages on independent directors for failure in audit committee supervision. The decision underscores that even independent directors may face civil consequences where due diligence obligations are not adequately discharged, subject to protection available under Section 149(12).
- 2. Misstatement in Prospectus (Section 35):** Section 35 imposes civil liability on directors for untrue statements or material omissions in a prospectus. Directors who authorize such issuance may be required to compensate investors who suffer losses upon relying on misleading disclosures. Although the provision is stringent, directors may avoid liability by proving reasonable belief in truth of the statement or timely withdrawal of consent.
- 3. Oppression and Mismanagement (Sections 241-242):** Under Sections 241 and 242, eligible members may approach the National Company Law Tribunal (NCLT) where company affairs are conducted in a manner oppressive to members or prejudicial to the company's interests. Although these provisions are remedial rather than strictly compensatory, they may result in civil consequences for directors, including removal from office or directors affecting their powers. The Tribunal possesses wide discretion to pass orders regulating the conduct of affairs, mandating share buyouts or restructuring management.
- 4. Liability in Related Party Transactions:** Section 188 governs related party transactions and requires proper disclosure, approval and adherence to arm's length principles.<sup>9</sup> Where directors enter into transactions involving personal interest without complying with statutory safeguards, such contracts may be rendered voidable at the option of the company.  
Directors may be required to indemnify the company for any losses arising from unfair or prejudicial terms. In case of listed entities, additional compliance under SEBI's Listing Obligations and Disclosure Requirements (LODR) Regulations strengthens scrutiny and accountability in related party dealings.
- 5. Compensation and Damages:** Civil damages are assessed on the basis of actual loss suffered by the company, including financial harm, overpayments or misapplication of assets. Directors may claim contribution from co-directors where liability is shared.

<sup>8</sup> Nexdigm. (n.d.). *Duties of Directors in India – Legal responsibilities & Governance guidelines* | Nexdigm. <https://www.nexdigm.com/doing-business-in-india/duties-of-directors.php>

<sup>9</sup> *Section 188. Related party transactions* | *Companies Act Integrated Ready Reckoner* | *Companies Act 2013* | CAIRR. (n.d.). *Companies Act Integrated Ready Reckoner* | *Companies Act 2013* | CAIRR. <https://ca2013.com/188-related-party-transactions/>

Section 197 also permits Directors and Officers (D&O) insurance for negligence-based liabilities, though such coverage does not extend to fraudulent or willful misconduct.

### **Criminal Liabilities of Directors**

Criminal liability under the Companies Act, 2013 is imposed in cases involving serious misconduct, fraud or willful statutory violations. Unlike civil liability, this is compensatory in nature and requires proof of guilty intent (*mens rea*) or conscious wrongdoing. These provisions are designed to deter conduct that undermines corporate integrity and public confidence. Prosecution may be initiated before special courts, NCLT or in coordination with regulatory authorities such as the Securities and Exchange Board of India.

#### **1. Fraud (Section 447)**

Section 447 prescribes stringent punishment for fraud, including imprisonment ranging from six months to ten years and fines extending up to three times the amount involved. Fraud is broadly defined to include acts, omissions, concealment of facts or abuse of position committed with the intent to deceive or cause wrongful gain or loss.

Directors may be held criminally liable where fraud is committed with their knowledge, consent, connivance or attributable neglect. The large-scale accounting manipulation in Satyam Computer Services (2009) led to custodial sentences for key executives, demonstrating the deterrent intent behind Section 447.

#### **2. False Statements (Section 448)**

Section 448 penalizes directors who knowingly make false statements or omit material facts in documents required under the Act, including financial statements, annual returns or filings before the NCLT. The punishment mirrors the severity of fraud under Section 447 where intentional falsification is established.

Courts may infer intent from surrounding circumstances, such as deliberate suppression of red flags or misrepresentation in compliance documents. In listed entities, SEBI may coordinate enforcement action where such misstatements affect investor interests.

#### **3. CSR Non-Compliance (Section 135)**

Section 135, read with its penal provisions, imposes consequences for willful failure to comply with Corporate Social Responsibility (CSR) obligations. Companies meeting prescribed financial thresholds must allocate the mandated CSR expenditure or transfer unspent amounts in accordance with statutory requirements.

Where directors deliberately default in compliance or divert funds, fines and prosecution may follow. However, liability generally arises in cases of non-compliance rather than genuine financial incapacity.

#### **4. Non-Maintenance of Books of Accounts (Section 128)**

Section 128 requires companies to maintain proper books of account reflecting true and fair financial position. Failure to do so, or deliberate falsification of records, may attract imprisonment ranging from six months to three years along with monetary fines.

Under Section 2(60), directors categorized as “officers in default” may be held liable unless they demonstrate lack of involvement or due diligence. Auditor reporting obligations often trigger regulatory scrutiny and investigation by the Registrar of Companies.

#### **5. Liability under SEBI Laws**

Directors of listed companies may also face criminal consequences under securities laws for insider tra-

ding, fraudulent inducement, market manipulation or non-disclosure of material information. The SEBI Act and related regulations prescribe substantial fines and imprisonment for serious violations.

In proceedings involving Manpasand Beverages Ltd. (2022), regulatory action illustrated how misstatements and concealment may attract parallel proceedings before SEBI and adjudicatory forums, reinforcing the multi-layered enforcement framework applicable to directors.<sup>10</sup>

### **Vicarious Liability and “Officer in Default”**

Under the corporate law vicarious liability refers to the attribution of a company’s wrongful acts to its directors not necessarily on the basis of direct personal involvement, but by virtue of their supervisory or controlling position. Under the Companies Act, 2013, such liability operates primarily through the statutory concept of the “officer in default” as defined in Section 2(60). Unlike civil tort principles, criminal vicarious liability in company law is not automatic; it arises only where the statute specifically provides for it and where a sufficient nexus between the director and the default is established.

### **Concept of Vicarious Liability**

In corporate criminal jurisprudence, directors are not presumed liable solely because they hold office. The Supreme Court in *Sunil Bharti Mittal vs CBI* (2015) clarified that there is no automatic criminal liability for directors unless a statute expressly creates such liability or evidence demonstrates active involvement, consent, connivance or neglect. The Court emphasized that criminal intent cannot be inferred merely from designation. This approach protects non-executive and independent directors from blanket prosecution while ensuring that those who exercise real control do not evade responsibility.

### **“Officer in Default” under Section 2(60)**

Section 2(60) introduces the statutory mechanism through which vicarious liability is operationalized. The provision defines “officer in default” in an inclusive manner, covering managing directors, whole-time directors, key managerial personnel such as CEO, CFO and Company Secretary, as well as any director who is aware of, participates in or consents to the contravention.

In certain cases, the provision extends liability collectively to all directors, unless a specific director can demonstrate lack of knowledge or due diligence. This creates a rebuttable presumption of responsibility, effectively placing a limited evidentiary burden on directors to establish non-involvement. However, independent directors benefit from the statutory safeguard under Section 149(12), which restricts their liability to acts committed with their knowledge, consent or lack of due diligence.

In *State of Madras v. C.V. Parekh*, the Supreme Court held that mere holding of office does not suffice; there must be evidence of control or responsibility in relation to the offense. Courts therefore require specific averments regarding the role played by the director before fastening liability.

### **Practical operation Across Offences**

In practice, the concept of “officer in default” is invoked across a range of statutory violations, including failure to file annual returns or financial statements, non-maintenance of books of accounts, CSR

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<sup>10</sup> *Analyzing Directors’ Duty of Care under the Companies Act, 2013*. (2023b, March 30). IndiaCorpLaw. <https://indiacorplaw.in/2023/03/29/analyzing-directors-duty-of-care-under-the-companies-act-2013/>

defaults and fraudulent conduct.<sup>11</sup> For procedural non-compliance, liability may extend to all directors unless delegated authority and absence of participation are demonstrated. In cases involving fraud under Section 447, knowledge or connivance must be specifically established.

### Defenses and Protectors Available to Directors

While the Companies Act, 2013 imposes significant civil and criminal liabilities on directors, it simultaneously provides safeguards to ensure that honest decision-making is not unduly penalized. These protections arise from statutory provisions, judicial doctrines, and contractual mechanisms, all of which seek to balance accountability with commercial practicality. The law recognizes that corporate decision-making inherently involve risk, and therefore shields directors from liability arising merely from unsuccessful outcomes. Defenses available are:

**1. Business Judgment Rule:** Indian jurisprudence has gradually acknowledgment the principles underlying the business judgment rule; a doctrine developed in common law jurisdictions. Under this rule, courts refrain from interfering with bona fide commercial decisions taken by directors, provided such decisions were made in good faith, with reasonable care, and for a legitimate business purpose. Judicial scrutiny focuses on decision-making process rather than the commercial wisdom of the outcome.

In *ICICI Bank Ltd. V. Piscean Investment & Finance Ltd.* (2022), the National Company Law Appellate Tribunal (NCLAT) emphasized that directors act after proper deliberation, consultation and documentation, they cannot be held liable merely because the transaction resulted in financial loss.

**2. Protection of Independent Directors (Section 149(12)):** Section 149(12) provides a statutory safeguard for independent directors by limiting their liability to acts committed with their knowledge, consent, connivance or where they failed to exercise due diligence. This provision significantly narrows the scope of vicarious liability otherwise contemplated under Section 2(60).

Independent directors are therefore not automatically responsible for operational defaults. Their protection depends upon demonstrating active participation in meetings, reasonable inquiry into suspicious transactions and discharge of committee responsibilities. Regulatory developments following proceedings such as *Manpasand Beverages Ltd.* (2022) have further clarified that independent directors are not liable for third-party fraud in the absence of personal complicity or neglect.

**3. Directors' and Officers' (D&O) Insurance:** Section 197 permits companies to obtain Directors' and Officers' (D&O) Insurance to indemnify directors against liabilities arising from negligence or breach of duty. Such insurance typically covers legal defense costs, settlements and damages awarded in civil proceedings. However, coverage does not extend to fraudulent or dishonest conduct, thereby preserving the deterrent purpose of criminal sanctions.

In practice, especially among listed companies, D&O insurance has become an important risk-management tool. It ensures that directors are not personally ruined for good-faith errors while maintaining accountability for deliberate wrongdoing.

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<sup>11</sup> Nalsar, T. L. F. (2025, November 5). *Machines, Middlemen, and Mandates: Vicarious Liability under the Companies Act, 2013 – Tech Law Forum @ NALSAR*. <https://techlawforum.nalsar.ac.in/machines-middlemen-and-mandates-vicarious-liability>

### **Emerging Issues and Contemporary Challenges**

The role of directors in India is evolving rapidly as corporate governance expands beyond traditional financial oversight. Developments such as environmental regulation, digital governance and the rise of startup ecosystems have significantly broadened the scope of director's responsibilities. Under the Companies Act, 2013 particularly under Section 166, directors are now expected to anticipate emerging risks and integrate them into broad-level decision making.

### **Liability in Startups and Unicorns**

The rapid growth of India's startup ecosystem has created new governance challenges for founder-directors and investors. High growth companies often prioritize innovation and rapid expansion, sometimes at the expense of strict regulatory compliance. However, directors of such companies remain subject to statutory obligations under the Companies act and may face vicarious liability under the "officer in default" framework.

In addition, startups that achieve large valuations may encounter regulatory scrutiny in areas such as financial disclosures, insolvency risks and investor protections. For instance, under the Insolvency and Bankruptcy Code, 2016, directors may be held liable for wrongful trading if they allow a company to continue operations despite insolvency risks. Venture capital nominees and shadow directors are also increasingly examined by the regulators where they exercise substantial influence over management decisions.

### **Digital Governance and Data Compliance**

Technological transformation has introduced new governance responsibilities for corporate boards. Directors are now expected to oversee issues such as cyber security issues, digital infrastructure, artificial intelligence governance and data protection compliance. Failure to exercise adequate oversight in these areas may expose directors to liability, particularly where data breaches or technological failures cause significant financial or reputational harm

The introduction of the Digital Personal Data Protection Act, 2023 has strengthened accountability for personal data management, imposing significant financial penalties for non-compliance. Alongside the Information Technology Act, 2000 and sectoral cyber security guidelines issued by financial regulators, these developments require boards to ensure effective data governance frameworks and risk management systems.

### **Increasing Regulatory Scrutiny**

Regulatory oversight of corporate governance has intensified in recent years. Authorities such as Ministry of Corporate Affairs and SEBI have adopted advanced monitoring mechanisms and stricter disclosure norms to detect irregularities in corporate conduct. Amendments to listing regulations, enhanced whistleblower protections and greater scrutiny of related party transactions have further expanded the compliance responsibilities of directors.

Tribunals and regulatory bodies have also demonstrated an increased willingness to impose penalties and disqualifications where governance standards are violated. This heightened enforcement environment underscores the need for directors to adopt proactive compliance and monitoring mechanism within corporate boards.

### **Liability in Climate Transitions and Green Finance**

Another emerging area of liability relates to climate governance and green finance. As companies increasingly issue green bonds or publish sustainability reports, directors may face scrutiny for “greenwashing”, which refers to misleading representations regarding environmental performance or climate commitments. Misstatements in such disclosures may attract penalties under securities laws and in extreme cases, fraud provisions under company law.

Consequently, directors must ensure that climate-related disclosures, sustainability targets and environmental reporting are supported by verifiable data and appropriate internal oversight mechanisms.

### **Forward-Looking Perspective**

These emerging developments indicate that the role of directors is shifting from that of passive compliance supervisors to strategic risk managers. Modern boards must integrate expertise in sustainability, digital governance and regulatory compliance to effectively navigate the evolving liability landscape. As corporate regulation continues to expand, directors will be expected to demonstrate not only legal compliance but also proactive leadership in addressing emerging governance risks.

### **Critical Analysis**

The expanding scope of directors’ duties under the Companies Act, 2013 reflects a shift from a shareholder-centric model to a broader stakeholder-oriented governance framework. While this evolution aligns Indian Corporate law with global standards, it simultaneously creates ambiguity and overextension of liability. Provisions such as Section 166, though progressive, remain open-textured, making it difficult for directors to clearly determine the extent of their obligations in areas like ESG compliance and digital governance.

A key concern lies in the overlapping regulatory framework, where authorities such as Securities and Exchange Board of India, the Ministry of Corporate Affairs and sectoral regulators impose parallel obligations. This multiplicity often leads to regulatory duplication and compliance fatigue, increasing the risk of inadvertent violations despite bona fide conduct. The rise of AI-driven surveillance and strict enforcement trends further intensifies this pressure, potentially discouraging qualified professionals from accepting directorial positions.

In the context of ESG and sustainability, the absence of clear, standardized benchmarks exposes directors to liability for evolving and sometimes subjective standards such as “greenwashing” or inadequate disclosures. While initiatives like BRSR aim to enhance transparency, they also risk creating a tick-box compliance culture, where substantive governance may be overshadowed by formal reporting requirements.

Similarly, in startups and high-growth companies, the law has not fully adapted to the informal and dynamic nature of entrepreneurial decision-making. Founder-directors and even investor nominees are increasingly subjected to traditional liability standards, which may be disproportionate in early-stage ecosystems where risk-taking is inherent and documentation practices are less formalized.

Digital governance introduces another layer of complexity. Directors are now expected to oversee cyber security, data protection, and emerging technologies despite often lacking technical expertise. This raises questions about the realistic limits of the duty of care, as imposing liability without corresponding capacity –building mechanisms may result in unfair attribution of fault.

## Conclusion

The Companies Act, 2013 marks a transformative step in strengthening corporate governance in India by clearly articulating the duties and liabilities of directors. By codifying fiduciary obligations under Section 166 and introducing structured accountability through provisions relating to civil and criminal liability, the Act has significantly enhanced transparency, responsibility and ethical conduct within corporate management. It has moved beyond the limitations of the earlier framework by recognizing the critical role directors play not only in managing companies but also in safeguarding stakeholders interests in an increasingly complex business environment.

At the same time, the Act establishes a comprehensive liability regime that encompasses both compensatory and punitive dimensions. Civil liabilities ensure restitution and protection of stakeholder interests, while criminal provisions serve as a strong deterrent against fraud and willful misconduct. The inclusion of the “officer in default” concept further expands the scope of accountability, ensuring that individuals responsible for corporate decisions cannot evade liability behind the corporate veil. However, the application of these provisions in practice often raises concern regarding overbreadth and the potential for disproportionate liability, particularly for non-executive and independent directors.

The legal framework also attempts to strike a balance by providing important safeguards such as the business judgment rule, statutory protections under Section 149(12), and the availability of Directors and Officers (D&O) insurance. These mechanisms recognize that corporate decision-making inherently involves risk and uncertainty and that director should not be penalized merely for bona fide commercial judgments that do not yield desired outcomes. Nevertheless, the effectiveness of these protections depends largely on consistent judicial interpretation and practical enforcement, which at times remains uneven regulatory and adjudicatory bodies.

Looking ahead, the evolving corporate landscape presents new and complex challenges that extend beyond traditional governance concerns. Issues such as ESG compliance, digital governance, data protection, and increased regulatory scrutiny are reshaping the expectations placed on directors. In this context, there is a pressing need for greater clarity in legal standards, harmonizing among regulatory authorities and continuous capacity-building for directors. A balanced and forward-looking approach—one that enforces accountability while enabling informed and risk-sensitive decision-making will be essential to ensure that the law not only deters misconduct but also supports effective and dynamic corporate governance in India.

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