

Quadrant II – Notes

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Module Name: Position, Appointment of Directors, Qualifications of Directors

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Introduction

King and Kingdom are inseparable. Neither does a king exist without a kingdom nor a kingdom without a king. In the same way, a company cannot exist without directors. A 'director' is defined under Section 2(34) of the Companies Act of 2013 as "director appointed to the Board of a company".

In general parlance, a director may be understood as a natural person vested with the duty of providing directions to the company in which he is appointed. Such directors can be categorized as the officer of the company. They share the responsibility of achieving the goals of such companies as is put forth in the Memorandum of Association of the Company and involve with the different levels of management in laying down divided tasks, execution, supervision and control of such tasks aimed at achieving the ultimate and short-term objectives of the company.

In India, the statute that governs the laws regarding the directors of the company is the Companies Act of 2013 and the Companies (Appointment and Qualification of Directors) Rules, 2014. The Companies Act in itself does not lay down a concrete-provisions on what are the qualifications to be achieved by an individual to rise up to the position of a Director. However, there is a list of

negative traits enlisted which provides for those who cannot be appointed as Directors.

Directors

The Company law requires that every company requires to have a Board of Directors whose composition will vary depending on the kind of company it is. A company that is public is required to have a minimum of three, a private company shall have a minimum of two and there shall be a single director in the case of One Person Company. The threshold limit being fifteen that may be subject to change provided there has been a special resolution passed in this regard.

There are different types of Directors like ordinary directors, managing directors, whole-time directors, alternate directors, additional directors, professional directors, independent directors, nominee directors, small shareholder's directors and so on. The different directors are appointed by various stakeholders through varied procedures. When the Articles of Association which is the document for the internal management of the company makes no note of the Directors of the company, the initial subscribers of the Memorandum of Association will hold the position of directors till the Annual General Meeting is conducted. They are termed as first directors. In the Annual General Meeting, several directors are appointed. The Board of Directors appoint directors such as additional, alternate, and casual. Directors are sometimes appointed by the By Central Government or National Company Law Tribunal or by third parties.

Qualification for Appointment of Directors

The Act has a dedicated provision which is Section 162 that underlines the reasons for which a person may not appoint as a director. There is no such provision regarding the qualification under the Act. However, requirements can be listed as below:

1. The person must have completed the age of eighteen or above.
2. Nationality can be that of Indian or otherwise.
3. The person should have his own Digital Signature Certificate (DSC) through which Director's Identification Number (DIN) shall be obtained.
4. The person has to furnish a written declaration expressing his consent to act in the position of Director and he is not a person who falls under the category of disqualified members.
5. There is no academic qualification that needs to be held by the person who is desirous of obtaining the directorship of a company.

In the case of **Saraswathi Vilasam Shanmugha Nandha Nidhi Ltd. v. V.S. Daiva Sigamami Mudaliar** (1950 SCC Online Mad 116) the Madras High Court has stated that "There is nothing in any provisions of the Companies Act which precludes a company from prescribing additional qualifications for directorship if the articles so provide. There is nothing unreasonable in having a non-statutory minimum age-limit for Directors with a view to justify confidence in mature judgment".

Rule 5 of The Companies (Appointment and Qualification of Directors) Rules, 2014 states the qualification of the Independent Director as follows

“An independent director shall possess appropriate skills, experience, and knowledge in one or more fields of finance, law, management, sales, marketing, administration, research, corporate governance, technical operations, or other disciplines related to the company’s business.”

Disqualifications for Appointment of Director

The relevant provision of the law that deals with the disqualification of directors are Section 152, 164, 165, and 188 of the Act and The Companies (Appointment and Qualification of Directors) Rules, 2014.

The grounds for Disqualification are mentioned as below:

1. Under Section 164 (1)

- i. Person will not hold eligibility for a directorship in the company if he has been declared to be a person with unsound mind by a competent court.
- ii. Person is insolvent and has undischarged liabilities or has a pending application in the court to be adjudged as insolvent.
- iii. The court has adjudged the person to be guilty of a crime involving moral turpitude. The sentence for the same being more than six months, the eligibility shall be withheld subject to passing of five years from such sentence. In the case of *Durga Singh v. State of Punjab*, the Punjab High Court elaborated on the meaning of moral turpitude and stated that “moral turpitude is anything done contrary to justice, honesty, principle or good morals, an act of baseness, vileness or depravity in the private and social duties which a man owes to his fellow men or society in general contrary to accepted and customary rule of right and duty between man and man”

- iv. If the sentence of his crime exceeds that of seven years. he shall be deemed ineligible for the post of director in any company.
- v. An order warranting the disqualification of the person is ruled by a competent court and during the application of such order, the person cannot become a director.
- vi. The person has failed to pay the amount due on his shares and a period of half a year has gone by without his paying the due.
- vii. The person has been involved in a related party transaction in the past five years.
- viii. The person cannot be appointed as a director unless he is allotted a Director's Identification Number (DIN)

2. Under Section 164 (2)

The person shall not be eligible for re-appointment in the company or any other company if such company has failed to furnish the returns or statement of finance consecutively for a period of three years or as stated in Section 164(2)(b) "has failed to repay the deposits accepted by it or pay interest thereon or 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"

3. Other Disqualifications

- i. Section 165 of the Act prohibits persons from holding the position of a director in more than twenty companies.

- ii. If the e-form DIR-3 KYC of the person who is a director is not filed, the directorship of such person will be disqualified.
- iii. If the e-form ACTIVE is not filed by the prescribed company, then the Directors of such company will be categorized as Director of ACTIVE non-compliant company.
- iv. Rule 7(8) of the Rules states that “No person shall hold the position of small shareholders’ director in more than two companies at the same time”. The second company must not be such that it is in a position to cause conflict with the first company or is a competitor of the first company.

Position of Directors

The position of a director of any corporate enterprise is a tough subject to explain (Ram Chand & Sons Sugar Mills Pvt. Ltd.v. Kanhayalal Bhargava AIR (1996) Cal). The position of a director has been given by L.J. Bowen in the case of Imperial Hydropathic Hotel Co Blackpool v. Hampson ((1883) 23 Ch D 1) the director has a versatile position in a corporate body. Directors are described as trustees, or as agents and sometimes even as managing partners. So the question that arises is what is the position of a director in the company whether he is a servant of the company or an agent or a trustee?

Are director’s servants of the company?

Considering directors as a servant of the company will be wrong as these are professional men and women of the company who are hired to direct the affairs of the company. A more adequate way to describe them is as officers of the company.

Directors as agents

It has been held that directors are agents of the company as the company is an artificial person it can act through directors only (Ferguson v. Wilson (1904) SLR 41 601). The relation of a director and the company is like an ordinary relation of principal and agent.

In the case of Indian Overseas Bank v. RM Marketing (AIR (2002) Delhi 344), it was held that the directors of a company could not be made liable merely because he is a director as he has not given any personal guarantee for a loan that has been taken by the company.

As directors are the agents of the company the company and agents share a relationship as such the directors are not personally liable for any transaction held on behalf of the company. Further, the directors have to disclose any personal interest vested in the company.

Directors as Trustees

Directors are not the trustees of the company, but they are treated as trustees where money and properties are involved as it is under their control. In the case of Ramaswamy Iyer v. Brahamayya & Co. (AIR 1965 Mad 176), it was held that in terms of their power of applying funds of the company and for misuse of power, the directors are liable as trustees and even after their death the liability remains as a cause of action survives against their legal representative.

Directors can be described as trustees due to their nature of the office as Directors are appointed to manage the affairs of the company for the benefit

of shareholders. The director of a company is not a trustee in his true form as a trustee of will or marriage settlement. As the director of the company is a paid officer of a company.

Now the question that arises is if the directors are trustees are they a trustee to the shareholders or to the company. The directors are the trustees of the company and not of shareholders and hence hold no fiduciary duty towards the shareholders.

Directors as organs of corporate body

It has been stated that the board of directors is the brain of the company and a company does its act through them

As a corporation has no mind or body of its own and its action is done by a person that is not merely an agent or trustee but by someone the company will be liable as his action is the action of the company itself. If a company is considered a human body, the directors are the mind and the will of the company as they control the actions of the company.

The position of a director is complicating one even though a director cannot be called a servant of the company it is called the officer or the controller of the company. Similarly, the director is not the trustee of the company he is a trustee in respect of money and property and the trustee of the company not of the shareholders. In true sense, the directors are the agent of the company and have a relationship as an agent and principal. Lastly, the director is the brain of the company