



THE COMPLIANCE & ETHICS ACADEMY

A Legasis Initiative

**Interactive session on Corporate Decision Making and Liabilities
- Suhas Tuljapurkar**



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Bhopal Gas Tragedy--- 1984

A Case Study on Corporate Liabilities

- The Company – A subsidiary UCIL
- The Owner – UCC (GoI also held some shares in UCIL)
- The Chairman of the Board & the Board
- Civil Liabilities
 - Compensation ... Settled by the SC in 1989 (\$ 470 M)
 - “Why did the Court not pronounce on certain important legal questions of far reaching importance said to arise in the appeals as to the principles of liability of monolithic, economically entrenched multi-national companies operating with inherently dangerous technologies in the developing countries of the third world--questions said to be of great contemporary relevance to the democracies of the third-world?”

BHOPAL GAS TRAGEDY
2nd-3rd December 1984
The Night of Death

le by-

BHOPAL DISASTER 1984 TO?
THE SUFFERING CONTINUES,
SO DOES THE STRUGGLE.
BHOPAL GAS PEEDIT MAHILA SATHIBHANGA
BHOPAL GAS PEEDIT MAHILA P...

Bhopal Gas Tragedy--- 1984

A Case Study on Corporate Liabilities

- Reactive Legislations
 - The Environment Protection Act, 1986
 - Concept of EIA resulted in EIA Notification 1994
 - Hazardous Waste (Management & Handling) Rules 1989
 - The Public Liability Insurance Act, 1991
 - The Factories Act Amendment 1987 (Occupier = Director)
 - doctrine of "*parens patriae*" (government's guardianship of citizens) -- The Bhopal Gas Disaster (Processing of Claims) Ordinance, 1985– Uncompensated abrogation of Fundamental Right (to Recourse)
- Judicial Activism
 - "Absolute Liability" principle by the SC (MC Mehta vs Uoi, 1989)
- Consequential Controversy on Nuclear Liabilities
 - The Civil Liability for Nuclear Damage Act, 2010 (CNLD Rules 2011)
- Criminal Liability
- Appeals are still pending.... 2 of the accused are dead.



Corporate Liabilities

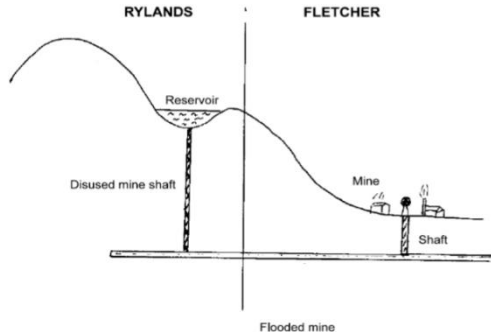




Corporate Liabilities

- Vicarious Liabilities
 - Employer is liable for the acts of the employees
 - Though an exception to Criminal Liabilities.... The Exception is critical
- Corporate Criminal Liabilities
- **Absolute Liability** Automatic Primary Liability
 - No mensrea required, due diligence is no defense
- **Strict Liability**
 - convicting a person for a regulatory offence on prima facie evidence but without proof of mensrea
- **Identification Doctrine...**
 - Directing Mind of a corporation
 - KMPs Liabilities
 - “Officer in Default”
 - Occupier-Director (Entire Board if a Director is not the Occupier)
 - Merger Doctrine...
 - Individual Promoter- Person merges with Company-
 - “ accustomed to act in accordance with the advice...

DIAGRAMMATICAL RERPRESENTATION



Corporate Liabilities....The Board of Directors

- Board of Directors as the Apex Group
 - Organizational Culpability is attributable to a group & not individuals
 - Knowledge is compartmentalized
 - Aggregation of Knowledge at the Board level
 - Statutory Responsibilities of the Board of Directors
- Fiduciary Duties of the Directors
 - Loyalty -- Duty to act in the interest of the Company
 - Duty of Care-
 - Duty of Disclosures
 - Duty of Extra Care
- Corporate Governance
- Oversight Risk
- Compliance Oversight



The Fiduciary Duty - Loyalty

- **Loyalty:** To act in the Interest of the Company
 - Consequential aspect: “Conflict of Interest” (Sec 188(1)(b), Sec 166 (4), Chp II Reg 4 of SEBI LODR, Reg 26)
 - Consequential aspect: “Composition of the Board- Appointment of Independent Directors, Woman Director” (Sec 149(1), (4) to 149(13), Sec 150(2) to 150(4), Schedule IV, Reg 17(6)(d) of SEBI LODR, Reg 25)
 - Consequential aspect: “Related Party Transactions” (Sec 188, Reg 23)
 - Consequential aspects: “Business Responsibility and Corporate Governance Report” (Reg 34(f), Reg 72)
- The Delhi High Court in its interim order (Rajeev Saumitra vs. Neetu Singh & Ors) held that a director is liable to pay to the company any undue gains realized from breach of duties prescribed by Section 166 of the Act.





"ALL THOSE IN FAVOR OF HAVING ANCHOVIES ON OUR PIZZA WILL SIGNIFY BY SAYING AYE."

The Fiduciary Duty – Due Care

- Care: Duty to pay attention and take due care
 - Consequential aspect: Oversight Duty (Sec 166, Reg 4(2)(f))
 - Consequential aspect: Committees (Sec 177, Sec 178, Sec 135, Reg 18 and Part C and D of Schedule II, Reg 21)
 - Consequential aspect: Financial Controls (Sec 177, Sec 134, Rule 10A of Companies (Audit and Auditors) Rules, 2014)
 - Consequential aspect: Compliance (Sec 134(5)(f))
 - Consequential aspect: Best Judgement Rule- Business decision taken in good faith and in the best interests of the company.



The Fiduciary Duty - Disclosure

- Disclosure: Disclose all material information
 - Consequential aspect: Mandated Disclosures v Material – Filings to be done with the ROC and Stock Exchange Filings: Suzlon Energy Limited: A total fine of Rs 1.1 Crore, including Rs 5 Lakh on the Company Secretary and Compliance Officer has been imposed as the Company failed to disclose price sensitive information as required under the listing regulations on more than one occasion (failure to make certain corporate announcements to Stock Exchanges about orders received by the Company).
 - Consequential aspect: Information Asymmetry – Reg 4(2)(b) & (c)
 - Consequential aspect: Policy and then delegate – (Sec 135(3)A, Reg 21, Reg 23, Reg 4(d)(iv), Clause (p) of sub-section (3) of Section 134, Reg 16(1) C, Sec 178, Reg 9, Reg 30(4)(ii), Reg 9, Reg 43A, Sch II Part D(A), Reg 17(5)A)





The Fiduciary Duty - Extra Care

- Extra Care: **Careful Scrutiny of decisions**: Event Based.
- Consequential aspect: Test for whether duty is met:
 - no clear test; careful scrutiny of decision process.
 - Restructuring, Acquisition, Amalgamation, Preferential Payments, Fraudulent Preference etc. (Sec 327, 328)

“Even against very honest persons, allegations can be made. Those days have gone when filing of the complaints was taken as serious aspersions on integrity.”

— Arun Mishra, J. in *Common Cause v. Union of India*, (2018) 9 SCC 382, para 121



The Governance Duty

- Ensuring that organizational activities are aligned in a way that supports the organization's business goals.
 - Board's Responsibility to set up
 - Commonsense Approach & Principles



The Risk Duty

➤ Board's Oversight : Management's Risk Appetite

Risk Fitness Quiz: How Do You Score?



Risk Assessment
1. How well do we identify, measure and document the threats/risks that could impact on the achievement of our business objectives?

SCORE /10

Risk Treatment
2. How well and how often do we reevaluate the effectiveness of our risk treatment strategies?

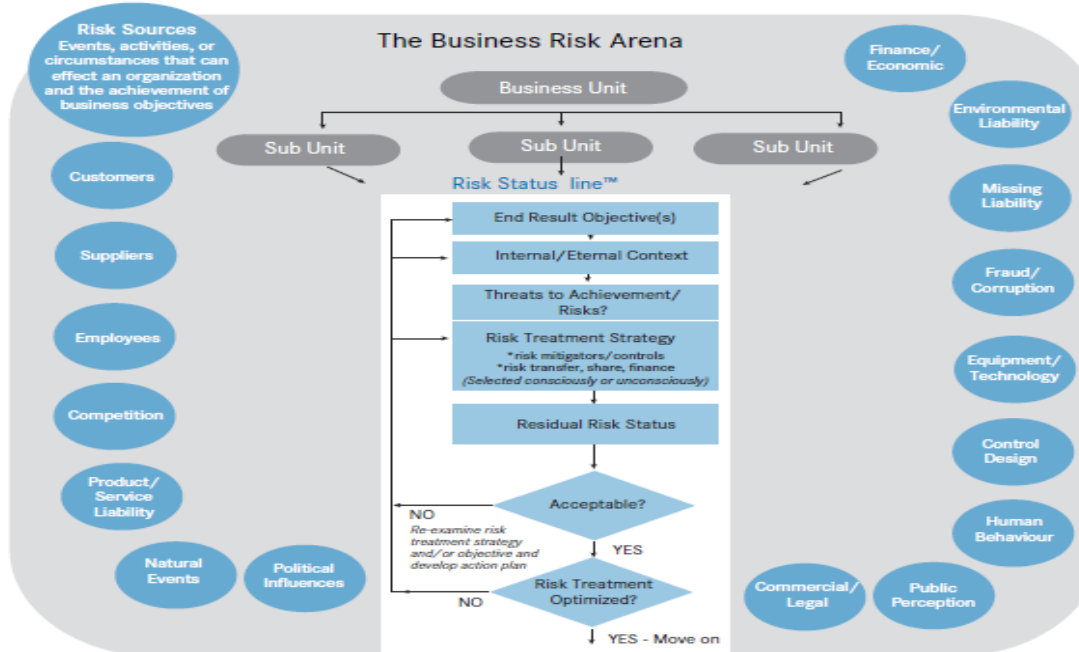
SCORE /10

Risk Treatment Optimization
3. How good are we at identifying opportunities to eliminate expensive risk treatments while still maintaining an acceptable residual risk level at a lower overall cost?

SCORE /10

Risk Testing the Future
4. How good are we at documenting and evaluating risks when making important business decisions, launching new products/services, and preparing strategic business plans?

SCORE /10



Risk Oversight Process
10. How well briefed is the Board of Directors and Senior Management on the company's significant residual risks? Have they taken steps to ensure work units are identifying, measuring, treating and monitoring significant risks?

SCORE /10

Regular Risk Re-evaluation
9. How effective is our corporate process to reassess the effectiveness of our risk management processes and periodically reassess the acceptability of risk acceptance decisions?

SCORE /10

Risk Transfer/Financing Options
8. How effective are we at identifying risk sharing and insurance options to avoid or reduce the consequences of specific threats/risks to business objectives?

SCORE /10

Early Warning Systems
7. How good are we at regularly monitoring our risk status using early warning signs that indicate changes might be needed to risk treatments and/or objectives?

SCORE /10

Planning for Serious Risk Situations
5. Do we have contingency plans in place to deal with potentially high risk but low probability situations that could cripple business units or the organization? Do we periodically revisit these plans to reassess their adequacy?

SCORE /10

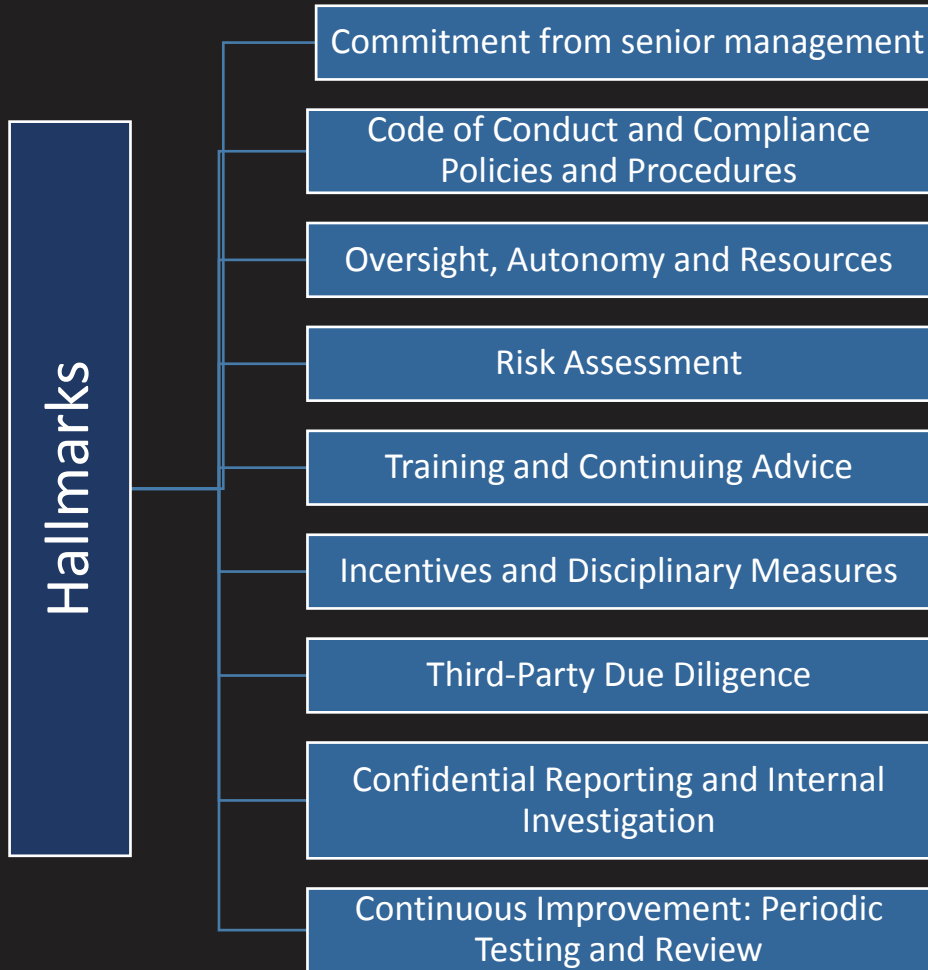
Worst Case Scenarios
6. How good are we at considering the possibility of high risk situations, which, if they occurred together, could have a devastating impact on the organization?

SCORE /10

TOTAL RISK FITNESS SCORE /100



The Compliance Duty



- Compliance with ALL laws
- Proper System: Adequate & Operating Effectively
- Non Prosecution
- Deferred Prosecution
- Risk Based Approach
 - Business Continuity vs Prosecution
- Standards of Systems
 - ISO 19600
 - ISO 37001



Statutory and Regulatory Landscape

1

2

3

Companies Act, 2013

- Section 166: Duties of Directors
- Schedule IV: Code of conduct of Independent Directors

SEBI (Listing Obligations and Disclosure Requirements) Reg, 2015

- Reg 4(2)(f): Responsibilities of the Board of Directors

Secretarial Standards

- Prescribe the procedural aspects of the duties of Directors



Delegation of Powers

What can't be delegated?



Statutory and Regulatory Provisions-delegation under CA

- The Board may, by a resolution passed at a meeting, delegate to any committee of directors, the MD, the Manager or any other principal officer of the Company the following powers on such conditions as it may specify:
 - to borrow monies;
 - to invest the funds of the company;
 - to grant loans or give guarantee or provide security in respect of loans
- Vide circular 19/2014 dated 12 June, 2014, MCA has clarified that the powers of the Board under Rule 6(2)(a) of Companies (Share Capital and Debentures) Rules, 2014, with regard to issuance of duplicate shares can be exercised by a committee of Directors. The committee of directors may exercise such powers subject to any regulations imposed by the Board in this regard.



Powers & Duties - What can't be delegated?

- The Directors' Responsibility Statement to invest the funds of the company;
in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;
- Section 143(3)(e)- Duty of the Auditor to include in the Auditor's Report as to whether, in his opinion, the financial statements comply with the accounting standards.
- the directors had selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the profit and loss of the company for that period;

Section 143(2) - Duty of the Auditor to include in the Auditor's Report, whether the said accounts, financial statements give a true and fair view of the state of the company's affairs as at the end of its financial year and profit or loss and cash flow for the year



Powers & Duties - What can't be delegated?

- **the directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;**
- Section 128- Every company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statement for every financial year
- Section 143(12) - If an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such amount or amounts, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time.
- **the directors had prepared the annual accounts on a going concern basis; and**
- Indian Accounting Standard (Ind AS) 1 - An entity shall prepare financial statements on a going concern basis unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so.



Powers & Duties - What can't be delegated?

- **the directors, in the case of a listed company, had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and were operating effectively.**
- Pursuant to Rule 10A of the Companies (Audit and Auditors) Rules, 2014, for the financial years commencing on or after 1st April, 2015, the report of the auditor shall state about existence of Internal Financial Controls with reference to financial statements and its operating effectiveness. – This enlarges the scope of the Auditor.
- **the directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively.**



THANK YOU

