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When Is a Director Personally Liable for the Company's Mistakes?

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ABSTRACT

A foundational principle of company law is that a company is treated as its own legal person, separate from those who manage it. This principle derives from Salomon v. A Salomon & Co. Ltd., and it explains why a director may take business risks, sign contracts, and even preside over a company's failure without necessarily incurring personal liability. Directors and shareholders are shielded by what is commonly called the corporate veil. That veil, however, was never intended to cover everything a director does, and courts and legislatures have over time carved out a set of situations in which it is lifted and the individual behind a decision is held personally responsible. This paper examines those situations in turn: beginning with the general rule of limited liability; then addressing the statutory provisions that impose liability on directors directly (for fraud, tax default, wrongful trading, and similar conduct); the case law on piercing the corporate veil where a company is used as a sham; the liability arising from breach of fiduciary duty or personal negligence; and, finally, the criminal liability attaching to "officers in default" under various statutes. Drawing on cases such as Gilford Motor Co. Ltd. v. Horne, Jones v. Lipman, and Williams v. Natural Life Health Foods Ltd., together with provisions of the Companies Act 2013, the Companies Act 2006, and the Insolvency Act 1986, this paper argues that none of this liability is automatic: it arises only once a director has stepped outside honest, careful, and authorised conduct.

Keywords: Director liability, Corporate veil, Separate legal personality

I. WHERE IT ALL STARTS: SEPARATE LEGAL PERSONALITY

Any discussion of director liability must begin from the same premise. Once a company is incorporated, it becomes its own legal person: it can own property, sign contracts, sue and be sued, and, importantly, it carries its own debts. The House of Lords made this principle largely unassailable in *Salomon v. A Salomon & Co. Ltd.*,¹ holding that even a company controlled almost entirely by one individual is not that individual's alter ego as far as the law is concerned. Indian courts have followed the same approach, treating the company as separate from its shareholders and directors.²

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¹ *Salomon v. A Salomon & Co. Ltd.* [1897] AC 22 (HL) (appeal taken from Eng.).

² *Life Insurance Corporation of India v. Escorts Ltd.*, (1986) 1 SCC 264 (India).

In practice, this means that a director who authorises a poor investment, backs a product that fails, or signs a contract the company cannot afford is usually not personally liable to creditors. This is, in essence, the point of incorporation: it allows individuals to take commercial risks without exposing personal assets to every business decision.

That said, limited liability protects only the company's mistakes; it does not protect a director's own wrongdoing. Once a director's conduct ceases to be an honest business misjudgment and becomes something the law independently disapproves of, such as fraud, personal negligence, or breach of a duty owed personally, the veil becomes largely irrelevant, because at that point the company's liability is no longer what is in issue.

II. STATUTORY LIABILITY: WHERE THE LEGISLATION PROVIDES DIRECTLY

The most direct exception to limited liability arises where a statute provides expressly that directors are to be personally liable in specified circumstances. Section 447 of the Companies Act 2013 renders any person, including a director, who is party to fraud connected with a company personally punishable with imprisonment and fine, without requiring any veil-piercing analysis.³ Section 166 goes further, setting out directors' duties of good faith and reasonable care, so that breach of those duties is independently actionable.⁴

Tax law operates on a similar principle, though the statutory basis has recently changed. Under section 179 of the Income-tax Act, 1961, where tax due from a private company could not be recovered, every person who had been a director of the company during the relevant previous year was jointly and severally liable for that tax, unless the director proved that the non-recovery could not be attributed to any gross neglect, misfeasance, or breach of duty on his or her part. The 1961 Act was repealed and replaced by the Income-tax Act, 2025, which took effect on 1 April 2026; section 179 of the 2025 Act is now a general anti-avoidance provision addressing impermissible avoidance arrangements and no longer deals with director liability for unpaid company tax, which is instead addressed, in substantially the same terms, in section 323 of the 2025 Act.⁵ The discussion above accordingly describes the position as it stood under section 179 of the repealed 1961 Act. Separately, section 141 of the Negotiable Instruments Act, 1881 extends criminal liability for a dishonoured cheque to anyone who was in charge of, and

³ Companies Act, 2013, § 447 (India).

⁴ Companies Act, 2013, § 166 (India).

⁵ Income-tax Act, 1961, § 179 (India) (repealed 2026); Income-tax Act, 2025, § 323 (India); *see also* Income-tax Act, 2025, § 179 (India) (impermissible avoidance arrangements).

responsible to the company for, the conduct of the company's business at the relevant time, subject to the limits the Supreme Court has read into that section.⁶

English law adopts a comparable approach. Section 172 of the Companies Act 2006 imposes a statutory duty on directors to promote the success of the company, and breach of that duty exposes a director to a claim by the company itself, which members may pursue on its behalf through a derivative claim.⁷ More significantly, section 214 of the Insolvency Act 1986 allows a liquidator to apply to court for an order that a director contribute personally to the company's assets where that director knew, or ought to have concluded, that there was no reasonable prospect of avoiding insolvent liquidation and failed to take every step available to minimise loss to creditors. This is the wrongful trading doctrine.⁸ What unites these provisions is that liability is never simply assumed: it must be proved against the specific director, usually by reference to what a reasonably diligent person in that role should have known or done.

III. PIERCING THE CORPORATE VEIL

Even in the absence of a specific statutory provision, courts retain an equitable power to look behind a company's structure where it has been used as a device to evade an existing legal obligation. *Gilford Motor Co. Ltd. v. Horne* is the paradigm case: an ex-employee bound by a restrictive covenant incorporated a company to solicit his former employer's customers, and the Court of Appeal treated the company as a mere cloak for his own breach and granted an injunction against both him and the company.⁹ In *Jones v. Lipman*, a vendor who had contracted to sell land transferred it to a company under his control solely to avoid an order for specific performance, and specific performance was ordered against both him and the company regardless; the judge famously described the company as "a mask which he holds before his face".¹⁰

In *DHN Food Distributors Ltd. v. Tower Hamlets London Borough Council*, the Court of Appeal similarly lifted the veil, treating a group of companies as a single economic unit for the purpose of assessing compensation, although subsequent decisions, notably *Adams v. Cape Industries plc*, have narrowed that reasoning considerably.¹¹ Indian courts apply the doctrine cautiously,

⁶ Negotiable Instruments Act, 1881, § 141 (India); *S.M.S. Pharmaceuticals Ltd. v. Neeta Bhalla*, (2005) 8 SCC 89 (India).

⁷ Companies Act 2006, c. 46, § 172 (UK); *see id.* § 170(1) (general duties owed by a director to the company); *id.* § 260 (derivative claims).

⁸ Insolvency Act 1986, c. 45, § 214 (UK).

⁹ *Gilford Motor Co. Ltd. v. Horne* [1933] Ch 935 (CA) (Eng.).

¹⁰ *Jones v. Lipman* [1962] 1 WLR 832 (Ch) (Eng.).

¹¹ *DHN Food Distributors Ltd. v. Tower Hamlets London Borough Council* [1976] 1 WLR 852 (CA) (Eng.); *Adams v. Cape Industries plc* [1990] Ch 433 (CA) (Eng.).

lifting the veil principally in cases involving tax evasion, evasion of a statute, or fraud on shareholders or creditors, rather than whenever a business happens to fail.¹²

IV. BREACH OF FIDUCIARY DUTY AND ACTING OUTSIDE AUTHORITY

Directors owe fiduciary duties to the company: to act in good faith, avoid conflicts of interest, refrain from making secret profits, and exercise independent judgment. Where a director appropriates a corporate opportunity, approves a related-party transaction from which the director personally benefits, or authorises payments beyond the director's authority, the company's decision-making is not truly in question; rather, the director is personally benefiting from, or responsible for, conduct that the company itself may sue to remedy. Because this form of liability concerns the individual's own conduct as a fiduciary, the corporate veil is not implicated: there is nothing to pierce, since the wrong was never the company's to begin with.

V. PERSONAL NEGLIGENCE, FRAUD AND MISREPRESENTATION

A director who gives advice or makes a representation to a third party may be sued in tort notwithstanding that the director was nominally acting on the company's behalf. In *Williams v. Natural Life Health Foods Ltd.*, the House of Lords held that a director is personally liable for a negligent misstatement only where the director has assumed personal responsibility for the advice and the claimant has reasonably relied on that assumption, rather than merely because the director was the company's guiding mind.¹³ This is a demanding threshold. Ordinary managerial decisions taken on the company's behalf do not, by themselves, create personal exposure in tort; what is required is something additional, such as a personal assurance, a fraudulent statement, or a guarantee given in the director's own name.

VI. CRIMINAL LIABILITY OF "OFFICERS IN DEFAULT"

A number of regulatory statutes impose criminal penalties on the company and, separately, on every "officer in default," a category that typically includes directors who knew of a contravention and either acquiesced in it or failed to exercise reasonable diligence to prevent it.¹⁴ The Supreme Court has made clear, however, that this form of vicarious criminal liability cannot be imposed on a director merely because of the office held: a director may be arraigned along with the company only where there is sufficient evidence of his or her active role in the offence coupled with criminal intent, or where the statute itself specifically provides for

¹² See *Life Insurance Corporation of India*, *supra* note 2, ¶ 90.

¹³ *Williams v. Natural Life Health Foods Ltd.* [1998] 1 WLR 830 (HL) (appeal taken from Eng.).

¹⁴ See, e.g., Companies Act, 2013, § 2(60) (India) (defining "officer who is in default"); Companies Act 2006, § 1121 (UK) (liability of officer in default).

vicarious liability.¹⁵ This protects nominee or non-executive directors who may have had no genuine operational involvement from being drawn into prosecutions intended for those actually responsible for running the company.

VII. OPPRESSION, MISMANAGEMENT AND WRONGFUL OR INSOLVENT TRADING

Where a company's affairs are conducted in a manner that is oppressive to minority shareholders or prejudicial to the company's own interests, the National Company Law Tribunal has broad powers under the Companies Act 2013 to make orders against the directors responsible, including orders for compensation.¹⁶ Once insolvency becomes a real prospect, the position changes further: continuing to trade and incur credit while aware that there is no realistic prospect of repayment can expose directors to liability for wrongful or fraudulent trading.¹⁷ At that stage, continuing to trade is no longer properly characterised as a business judgment; it amounts to a choice to shift the company's losses onto its creditors.

VIII. CONCLUSION

The idea running through this discussion is that the corporate veil protects decisions made honestly, and within a director's authority, for the company's benefit, but it was never intended to protect a director's own fraud, negligence, or deliberate misuse of the corporate structure. Courts and legislatures appear to have been careful not to allow this exception to swallow the general rule of limited liability, since a director who fears personal ruin over every ordinary business misjudgment will be discouraged from taking the risks that operating a business requires. The line, therefore, is not whether the company failed, but whether the director was at fault. A company's mistake remains the company's own problem until the point at which a director's own conduct, whether fraudulent, negligent, or a knowing breach of duty, becomes the true cause of the harm.

¹⁵ *Sunil Bharti Mittal v. Central Bureau of Investigation*, (2015) 4 SCC 609 (India).

¹⁶ Companies Act, 2013, §§ 241–246 (India); *see id.* § 242(2)(i) (recovery of undue gains made by a director); *id.* § 245(1)(g) (class action for damages or compensation against directors).

¹⁷ *See* Insolvency Act 1986, §§ 213–214 (UK).