

Loan to directors, etc.

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Coverage

- **Intent of the section**
- **Language of law**
- **Prohibited, restricted and un-restricted list**
- **Applicability**
- **Punishment provisions**

Intent of the Section



- Ensure that directors do not surpass their fiduciary duty towards the company for their own benefit

Loan to Directors, etc.

- **Loan- loan** including loan represented by **book debt, guarantee or security [LGS]**
- **To-** Loan/ guarantee/ security flowing from the Company
- **Directors**
- **Etc.-** list of persons are included here [explained later]

Section 185

Section 185 [1]-**Prohibitive list**

Company shall not, **directly** or **indirectly**, advance any loan, including any loan represented by **book debt** or guarantee or security in respect of any loan [LGS] to:

- Any director/ director of the holding company/ partner or **relative** of **such** director; or
- Any firm in which any **such** director is a partner.











Who is a relative?

Section 2[77] of CA,13

- Members of HUF
- Husband/wife
- Father
- Mother
- Brother
- Sister
- Son
- Son's wife
- Daughter
- Daughter's husband

Section 185

Illustrations: Does Section 185 allow LGS to:

 <p>Mr. A Director of X Ltd</p>	<p>Director- NO</p>	 <p>Mr. C Director of holding company of X Ltd</p>	<p>Director of holding company- NO</p>
 <p>Mrs. A Spouse of Mr. A</p>	<p>Relative of director- NO</p>	 <p>Mrs. c Spouse of Mr. C</p>	<p>Relative of director of holding company- NO</p>
 <p>Mr. B Partner of Mr. A</p>	<p>Partner of director- NO</p>	 <p>Mr. D Partner of Mr. C</p>	<p>Partner of director of holding company- NO</p>
 <p>Mrs. B Spouse of Mr. B</p>	<p>Relative of director's partner- YES</p>	 <p>Mrs. D Spouse of Mr. D</p>	<p>Relative of holding company director's partner- YES</p>

Section 185

Illustrations: Does Section 185 allow LGS to:

AB & Co. [where Mr. A is a partner]	Firm in which director is a partner- NO	CD & Co. [where Mr. C is a partner]	Firm in which director of the holding company is a partner- NO
BZ & Co. [where Mr. B is a partner]	Firm in which holding company's director partner is a partner- YES	DE & Co. [where Mr. D is a partner]	Firm in which holding company's director partner is a partner- YES

Section 185

Section 185 [2]-Restrictive list

Company may advance LGS to any person in whom director of the company is **interested** subject to the following conditions:

- **Special resolution** is passed at the General Meeting [disclosing full particulars of the LGS to be advanced and the purpose for which it is to be utilized in the explanatory statement to the notice];

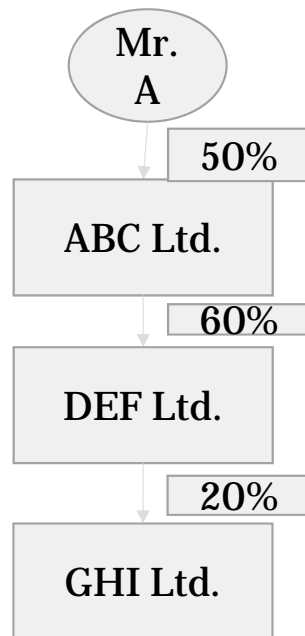
AND

- Loan is utilized for its principal business activities.

Person in whom director of the company is **interested**

- any **private company** of which any such director is a director or member
- any body corporate at a general meeting of which not less than **twenty-five per cent.** of the total voting power may be exercised or controlled by any such director, or by two or more such directors, together
- any body corporate, the BoD/ MD/ manager, whereof is **accustomed to act** in accordance with the directions or instructions of the Board, or of any director or directors, of the lending company.

Computing voting power for Section 185



In the given case, Mr. A holds 50% in ABC Ltd. which in turn is holding 60% in DEF Ltd. 20% of GHI Ltd. is held by DEF Ltd.

Mr. A's voting power shall be

- 50% in ABC Ltd.;
- 30% in DEF Ltd. [$50\% * 60\%$] and
- 6% IN GHI Ltd. [$50\% * 60\% * 20\%$]

Accordingly, ABC Ltd and DEF Ltd. shall be the persons in whom director of the company is interested. GHI Ltd. will not be deemed to be the persons in whom director is interested

Section 185

Section 185 [3]-Unrestricted list

Restrictions/prohibitions u/s 185[1] and [2] shall not apply [till Section 186] to:

- Loan to MD/WTD:
 - As conditions of service extended to all its employees;
 - Pursuant to a scheme approved by SR
- Companies providing LGS in their ordinary course of business where interest charged not less than prevailing yield of G sec of 1 year, 3 year, 5 year or 10 year
- LGS provided by holding to WOS [for principal business activities]
- Guarantee or security provided by holding to its subsidiary [for principal business activities]

Applicability [1/2]

Private Company	Which satisfies all three conditions: <ul style="list-style-type: none">- No investment has been done by any body corporate- Borrowing from banks/ FIs/ body corporate is less than lower of :<ul style="list-style-type: none">- Twice of paid up capital- Fifty crore rupees- It has no default in repayment of borrowings subsisting at the time of transaction	No
	Others	Yes
Public Company		Yes
Deemed Public Company		Yes

Applicability [2/2]

Govt. Company	<p>which satisfies both conditions:</p> <ul style="list-style-type: none"> - obtains approval from ministry administratively in charge of the company/ SG before making any LGS - Which has not defaulted in filing financial statements and annual return with the registrar 	No
	others	Yes
Nidhi Company	<p>-While granting loan to director/ relative in their capacity as members</p> <p style="text-align: center;">AND</p> <p>-Such transaction is disclosed in the annual accounts</p>	No
	Others	Yes

Punishment provisions

Company

Rs. 5 lakhs to Rs. 25 lakhs

Officer in default

**Imprisonment upto 6 months OR
fine Rs. 5 lakhs to Rs. 25 lakhs**

**Director or the person to whom the
loan is advanced**

**Imprisonment upto 6 months OR
fine Rs. 5 lakhs to Rs. 25 lakhs**

Thank You..