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Director's Liability Revisited: Supreme Court Clarifies the Limits of Vicarious Responsibility Across Fiscal Laws



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1. Introduction

The decision of the Hon'ble Supreme Court in *Saroj Pandey v. Govt. Of Nct Of Delhi* [2026] 185 taxmann.com 280 (SC) is a significant pronouncement on the nuanced issue of liability of directors under fiscal and penal laws. At a time when regulatory enforcement is becoming increasingly stringent, the judgment provides much-needed clarity on the extent to which individuals occupying managerial positions can be fastened with liability for acts of a company.

The judgment lays down the boundaries to the extent to which directors are liable and more specifically when they are not liable for the act of the Company being a separate legal entity. Though rendered in the context of Section 138 and 141 of the Negotiable Instruments Act, 1881 ("N.I. Act"), commonly associated with cheque dishonour cases, the underlying reasoning transcends the statute. The principles articulated by the Court are of wider relevance and have direct bearing on fiscal statutes, including the CGST Act, where similar provisions impose vicarious liability.

2. Concept of Separate Legal Entity and Role of Directors

The doctrine of separate legal entity, firmly embedded in company law jurisprudence since the landmark decision of the House of Lords in *Salomon v. Salomon (1897) A.C. 22* followed by the Indian Supreme Court in a plethora of judgements including in the famous *Vodafone International Holdings B.V. v. Union of India* [2012] 17 taxmann.com 202 (SC)/[2012] 204 Taxman 408 (SC)/[2012] 341 ITR 1 (SC), recognises a company as a juristic person distinct from its shareholders and directors. This principle has significant implications in fiscal jurisprudence as well, where the company is treated as an independent taxable entity, capable of owning property, incurring liabilities, and being assessed in its own name. Consequently, tax obligations—whether under direct or indirect tax regimes—are ordinarily fastened upon the company itself, and not upon those who manage its affairs. The sanctity of this principle ensures commercial certainty and facilitates risk-taking by insulating individuals from personal exposure arising out of corporate operations.

However, the role of directors introduces a nuanced dimension to this doctrine. While directors act as the "directing mind and will" of the company, their liability in tax matters is not automatic but arises only in specific statutory or exceptional circumstances. Tax statutes, including provisions under the Income-tax Act and GST laws, carve out limited situations where directors may be held personally liable—typically where there is evidence of fraud, wilful default, misfeasance, or where statutory dues cannot be recovered from the company. Even in such cases, the law requires strict compliance with conditions precedent before piercing the corporate veil, thereby maintaining a careful balance between accountability and the foundational principle of separate legal personality.

Judicial trends have consistently underscored that lifting the corporate veil is an exception rather than the rule, to be invoked sparingly and only where the corporate form is abused to evade tax or perpetrate illegality. Courts have cautioned against a routine attribution of liability to directors merely on account of their position, emphasising that vicarious liability must be expressly provided by statute and cannot be inferred. Thus, while directors play a central role in corporate governance and decision-making, their personal exposure in tax matters remains circumscribed, reinforcing that the company—being a separate legal entity—continues to bear primary responsibility for its fiscal obligations.

3. Factual Background

Coming to the case in hand, the appellant was one of the directors of the accused company which had issued cheques towards payment for supply of goods. The cheques were dishonoured upon presentation, following which statutory notice was issued and criminal proceedings were initiated. The director was arrayed as an accused primarily on the ground that she had signed a Board Resolution, which, according to the complainant, demonstrated her involvement in the affairs of the company. This reasoning found favour both with the Magistrate and the High Court, leading to the continuation of proceedings against her.

4. Provision Relating to Prosecution of Director

Section 141 of the N.I. Act, provides the statutory framework for fastening vicarious liability upon directors and officers of a company. The provision makes it clear that liability is not automatic but conditional upon the person being “in charge of” and “responsible to” the company for the conduct of its business at the relevant time. The provisos further carve out safeguards, including absence of knowledge and exercise of due diligence.

A striking feature of the present discussion is the similarity between Section 141 of the N.I. Act and Section 137 of the CGST Act. Both provisions employ nearly identical language in attributing liability to persons in charge of and responsible for the conduct of business, while also recognising defences based on lack of knowledge and due diligence.

That on a plain reading of the said provisions it can be seen that the provisions of the CGST Act are in pari-materia to the provision of the N.I. Act. Therefore, the jurisprudence on directors’ liability as developed under the N.I. Act assumes considerable relevance in interpreting analogous provisions under GST law.

5. Discussion & Findings of the Supreme Court

5.1 On the Law Relating to Prosecution of Directors

The Court reiterated that the law governing prosecutions under Section 138 read with Section 141 of the N.I. Act is well settled. It emphasised that a complaint must contain specific averments demonstrating that the accused was in charge of and responsible for the conduct of the business of the company at the time of the offence. Absent such foundational pleadings, the prosecution cannot be sustained.

5.2 Regarding No Deeming Liability on Account of Being a Director

A crucial clarification made by the Court is that merely holding the position of a director does not automatically attract liability. There is no deemed liability in law solely on account of designation. The requirement of Section 141 is substantive and must be satisfied through clear and specific allegations establishing active responsibility.

5.3 Regarding Signing of Board Resolution and Day-to-Day Affairs

The Court decisively rejected the reasoning that signing a Board Resolution ipso facto establishes involvement in day-to-day management. It observed that Board Resolutions pertain to policy-level decisions and cannot be equated with operational control. In the absence of specific allegations indicating direct participation in the conduct of business, such a basis is insufficient to attract criminal liability.

6. Application of Principles to the Present Case

Applying the above principles, the Supreme Court found that there was no material to show that the appellant was in charge of and responsible for the conduct of the business of the company. The complaint lacked the necessary averments, and the reliance placed solely on the signing of a Board Resolution was misplaced.

The Court noted that criminal liability, particularly vicarious liability, cannot be imposed in a mechanical or casual manner. In the absence of specific allegations and supporting material, the continuation of proceedings would amount to an abuse of process. Accordingly, the proceedings against the appellant were quashed, reinforcing the principle that liability must be founded on role and responsibility, not merely on designation.

7. Conclusion

The judgment marks an important reaffirmation of the limits of vicarious liability in corporate jurisprudence. It preserves the delicate balance between ensuring accountability of those who are genuinely responsible for corporate conduct and protecting individuals from unwarranted prosecution merely due to their formal association with a company.

Equally, the ruling serves as a reminder that criminal law cannot be stretched to compensate for deficiencies in pleadings or evidence. The insistence on specific averments and demonstrable involvement ensures that prosecutions remain grounded in legal principle rather than assumption. In doing so, the Court has strengthened the integrity of both corporate law and criminal jurisprudence.

8. Lessons from the Judgment

The decision underscores that liability of directors is not a matter of presumption but of proof. It highlights the necessity of carefully drafted complaints, clearly identifying the role of each accused. For companies and their boards, the judgment provides reassurance that participation in governance, without involvement in day-to-day operations, does not automatically expose directors to liability.

At the same time, it reinforces that those who are actively in control cannot evade responsibility behind the corporate veil. Importantly, the ruling assumes even greater significance in the context of independent directors. It implies, in principle, that independent and non-executive directors—whose role is largely supervisory and advisory—cannot be routinely implicated in proceedings in the absence of specific material demonstrating their involvement in the conduct of business or their consent, connivance, or negligence. Mere presence on the Board, participation in meetings, or approval of resolutions in a governance capacity cannot, by itself, trigger liability. This serves as a crucial safeguard to ensure that independent and non-executive directors are not deterred from discharging their oversight functions due to the risk of unwarranted prosecution, while still preserving accountability in cases where there is demonstrable complicity or failure of due diligence.

9. Applicability under GST Law

The relevance of this judgment in the GST context is both immediate and substantial. Section 137 of the CGST Act mirrors the language of Section 141 of the N.I. Act, and therefore the interpretative principles laid down by the Supreme Court would squarely apply. Authorities seeking to fasten liability on directors must demonstrate, through clear allegations and evidence, that such persons were in charge of and responsible for the conduct of business at the relevant time.

Importantly, the judgment strengthens the position that **mere designation as a director is insufficient to invoke penal provisions under GST laws**. In the absence of specific material indicating involvement, consent, connivance, or negligence, proceedings against directors would be legally unsustainable. This ensures that while genuine cases of evasion and misconduct are addressed, the corporate form is not disregarded lightly, thereby maintaining the foundational principle of separate legal personality within the GST regime.

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