

(1977) 03 DEL CK 0011

In the Delhi High Court

Case No : Civil Petition No. 46 of 1976

Om Prakash Khaitan

APPELLANT

Vs

Shree Keshariya Investment Ltd and Others

RESPONDENT

Date of Decision : 01-03-1977

Acts Referred:

Citation : (1978) 48 CompCas 85 : (1977) 13 DLT 382 : (1977) 2 ILR Delhi 470

Hon'ble Judges : H.L. Anand, J

Bench : Single Bench

Advocate : N.R. Khaitan, T.M. Sen, B. Mohan, Harish Chandra, H.S. Bhatia and A.P. Gupta, for the Appellant;

Judgement

H.L. Anand, J.

(1) OM Prakash Khaitan, Solicitor, who was a Director of Shree Keshariya Investment Limited during the material period, seeks relief u/s 633 of the Companies Act, 1956 (for short "the Act"), from liability arising out of a number of defaults and breaches committed by the Company in relation to its obligations under the Employees Provident Fund Act, Sales Tax Act, Employees State Insurance Act, Indian Textiles (Control) Order, Essential Commodities Act, and the Act, on the ground that since November 26, 1974 he ceased to be the Director of the Company ; that he was a Director of the Company by virtue of being its legal adviser and never took any active part in the management and the affairs of the Company; that he was on the Board of a number of Companies as such legal adviser but has not concerned himself with the day to day affairs of the Company or its management; and that he has always acted honestly and reasonably and has given proper advice to the management to act in accordance with law in relation to matters that were brought before the Board.

(2) The application is opposed by the various authorities, including the Registrar of Companies, primarily on the ground that by virtue of being a Director of the Company the petitioner was liable for the various defaults and breaches of which

the Company was guilty and that if the petitioner acted honestly or the breaches and defaults were committed in spite of the efforts of the petitioner to the contrary the petitioner would be discharged from obligation in appropriate proceedings and there was, Therefore, no ground to relieve the petitioner of the liability in the present proceedings.

(3) In his affidavit of February 19, 1977 the petitioner has given details of the defaults and breaches, which have since become subject matter of prosecutions, pending in the Magistrate's court in Baroda and Ahmedabad. In para 8 of the affidavit he has also specified the defaults and breaches in respect of which he apprehends proceedings. It was not disputed on behalf of the petitioner that this Court has no jurisdiction with regard to the criminal liability arising out of defaults and breaches which have already become subject matter of prosecution and that for any relief in relation to such defaults etc. the proper remedy of the petitioner would be an application under sub-section (1) of Section 633 to the Court hearing the cases. The only question that, Therefore, requires consideration is whether there is a case for the petitioner being excused under sub-section (2) of Section 633 of the Act of liability on account of defaults and breaches of the Company in respect of which proceedings are apprehended.

(4) Section 633 of the Act empowers the Court to give relief where it is satisfied that the officer of a Company, even though technically guilty of negligence, breach of duty, misfeasance or breach of trust or otherwise liable on account of any default or breach of the Company has nevertheless acted honestly and reasonably and that having regard to all the circumstances of the case, "including those connected with his appointment", he ought fairly to be excused. The object of the section appears to be to provide against undue hardship in deserving causes and to give relief from liability to persons who, though liable in law, ought to be excused rather than be allowed to be subjected to legal proceedings.

(5) It is true that when a person agrees to be appointed to the Board of Directors of a Company he is expected to exercise legitimate control over the management and the affairs of the Company and be conscious of his responsibility as such Director. It is also beyond doubt that when persons, who have distinguished themselves in various fields such as law, audit, management, financial management or who otherwise represent special interests on Boards such as the representatives of financial institutions. Government or Semi-Government bodies are appointed to the Boards it certainly gives a favorable projection to the management of the Company and holds out a tacit assurance to all those who would deal with the Company, including the prospective share-holders of the Company, that there are independent persons of eminence having specialised skill on the Board of the Company and that the affairs and management of the Company would, Therefore, be properly conducted in accordance with law. Unfortunately, however, most of such persons either do not actively participate in the management of the Company and its affairs or are unable on account of the

obvious limitation of the power of a Director and the principle of limited accountability incorporated in the Act, to exercise an effective control over the management and affairs of the Company with the result that the safeguard built into the corporate system by the institution of such directors becomes almost illusory. In the circumstances it is necessary to make a distinction between the directors, who are on the Board, purely by virtue of their technical skill or because they represent certain special interests and those who are in the effective control of the management and affairs of the Company, whether or not, they have any financial stakes in it, in determining if relief from liability arising out of the breaches and defaults of the Company should be granted or not. It cannot be denied that independent directors from the professions or from among the financial consultants or those that represent different interests, such as the financial institutions, have a salutary effect on the management of a Company in spite of the various legal constraints and limitations and if such a distinction is not made it is likely to scare such persons away from any possible association with the Company as directors. It is, Therefore, unreasonable to fasten liability on directors for the defaults and breaches of a Company where such directors are either the nominee directors or are appointed by virtue of their special skill or expertise. It is also unfortunate that with the limited accountability an effective control of the management of the affairs of a Company by the Board is not possible. While there is a strong case for urgent legislative action, both in the matter of widening the frontiers of accountability of a company, both to its Board of Directors and to the members, as also in relieving the special category of directors from consequences of default and breaches of the Company, judicial moderation is necessary in the administration of Section 633 of the Act so as to ensure that such categories of Directors are not subjected to the harassment of legal proceedings for breaches and defaults of a Company, which may at times be rather protracted. It would be proper in such cases to relieve such directors of consequences of the defaults and the breaches unless they are directly involved in the acts or omission complained of or have otherwise not acted honestly or reasonably or have financial involvement in the company.

(6) Having regard, Therefore, to the fact that the petitioner has been a Director of the Company, as indeed of a number of other Companies, by virtue of being a solicitor and did not participate in the management of the Company and had no financial involvement in it, I would relieve the petitioner of the liability arising out of breaches and defaults on the basis of which the petitioner apprehends proceedings.