

(1982) 03 BOM CK 0017

In the Bombay High Court

Case No : Company Petition No. 764 of 1981

Union of India and another

APPELLANT

Vs

Shri Changdeo Sugar Mills Ltd.

RESPONDENT

Date of Decision : 09-03-1982

Acts Referred:

Companies Act, 1956 — Section 408, 408(1), 408(5)

Citation : (1984) 55 CompCas 42

Hon'ble Judges : Aggarwal, J

Bench : Single Bench

Judgement

1. The petitioners are seeking directions (i) that the directors appointed by them under s. 408(1) of the Companies Act, 1956, by order dated November 17, 1973, continue to be the directors of the respondent company until they have completed their full of three years, and (ii) the board of directors elected by the company requires confirmation of their appointment under s. 408(5) of the Companies Act, 1956.

2. The background of the petition and the facts leading to its filing can be narrated briefly as follows :

3. By order dated November 17, 1973, made by the Government of India, Ministry of Law, Justice and Company Affairs, Department of Company Affairs, passed under s. 408(1) two directors were appointed for a period of three years. The validity of the said order was challenged in a writ petition being Misc. Petition No. 1306 of 1973, filed by the company and its two directors against the Union of India and others. By an order dated January 10, 1974, the directors appointed by the Central Govt. were restrained from taking any further steps or action in furtherance or implementation of the said order on the petitioners giving an undertaking, inter alia, not to call any meeting of the board of directors without the orders of the court. The undertaking was modified by order dated March 15, 1974, but that is not material for us. The Revenue Department in order to recover its tax dues had a receiver appointed of the business of the company and

this appointment came to an end on June 29, 1977. Thereafter, a notice of Motion No. 1154 of 1971, dated November 3, 1977, was taken out in the said writ petition to modify the said undertaking to enable the company, firstly, to call a meeting for appointing four new directors, secondly, to permit the board of directors to accept resignations of the old directors, and, thirdly, to empower the reconstituted board of directors to convene a meeting to carry on day-to-day business of the company and to borrow money from the Bank of Madura. The following order dated November 15, 1977, came to be passed by Mr. Justice Deshmukh (as she then was) :

"For a limited period of three months or the event occurring in para 8, whichever is later a board of directors is being constituted which shall consist of Shri Sitaram Dwarkadas Morarka - respondent No. 9, (2) Maj. Gen. R. K. Batra (Retired), (3) Shri T. Kannapan, Jt. Managing Director of Saroja Mills Ltd., Kappalur, (4) Two directors to be appointed by respondent No. 1 under the provisions of section 408 of the Companies Act, 1956, and (5) Two more directors to be nominated by the Bank of Madura after the loan of Rs. 90 lakhs is sanctioned by the bank.

The first meeting of the first five directors to be held at 4 p.m. on Saturday the 19th instant, at Bombay, at respondent No. 8-company's registered office at 123, M.G. Road, Bombay. Respondent No. 1 - Union of India and its Company Law Board - is expected to appoint the two directors under s. 408 before the time and date of the meeting. However, the persons to be so appointed should be any other persons than respondents Nos. 6 and 7. Respondent No. 8 - company's officers will forthwith prepare a notice of the first meeting together with the agenda and forward to respondent No. 1 for being served with their nominees.

In this first meeting, the only business to be transacted will be to pass a resolution for obtaining loan from the Bank of Madura, to the extent of Rs. 90 lakhs on the basis of and in the light of the letter of the respondent No. 8 company, dated 22nd October, 1977, of which a copy has been over to the counsel for respondent No. 1. They will not transact any other business in that meeting.

In this first meeting the members present will elect their own chairman for the purpose of supervising and conducting the business of that meeting only.

After the loan is sanctioned the bank will have the right to nominate two directors as proposed by them in the earlier negotiations. Out of these two nominees of the bank, nominee No. 1 will be the chairman of the board if directors of 7 members during the remaining period of the life of that board. After the full board of 7 members is so constituted, they will have all the powers under the Companies Act as a board of directors for conducting the affairs of the company.

This board will meet at least once in a fortnight. The fortnight is being calculated

as the first 15 days of the calendar month and the remaining days of the calendar month constituting the two fortnights.

This board is further under an obligation to get the accounts of the company audited and call an annual general meeting within the period of three months.

Once the annual general meeting so held elects its own board of directors, this board will cease to function as such except that the bank's two nominees as creditors-representative will continue as directors of the board, subject, however, to the general provisions of the Companies Act.

To avoid misunderstanding it is clarified that nominee No. 1 of the bank appointed as chairman is only during the limited period as mentioned in para. 1 and elected board will be free to act according to the provisions of the Companies Act.

The appointment of the two directors under s. 408 in pursuance of this order will also come to an end along with the life of this temporary board. However, it is the contention of the Union of India that in view of the earlier appointment of respondents. Nos. 6 and 7, which is under dispute, the new board to be elected will have to allow the provisions of s. 408(5) of the Companies Act. This position is being disputed by the petitioner, respondent No. 9 and the company. The only direction I choose to give is that at this stage the persons concerned will act according to law, and this order is being passed without prejudice to the rights and contentions of either party.

After operation of this order and the life of the board created under this order comes to an end, liberty to respondent No. 1 to apply for vacating the and interim order dated 10th January, 1974, as modified by order dated 15th March, 1974."

4. Acting on the said order, the Central Govt. by its letter dated 17th November, 1977 intimated to the company the names of two directors. The Bank of Madura also nominated a director.

5. Thereafter, the company took out various notices of motion for extension of time; the last of them was the notice of Motion No. 900 of 1980. This notice of motion along with the main writ petition were heard by me and by my judgment and order dated 12th September, 1980, the writ petition was dismissed and rule discharged, while giving certain directions on the notice of motion.

6. After the disposal of the writ petition, an annual general meeting of the company was held on 30th September, 1981, whereat Shri Sitaram D. Morarka, Shri S. K. Wankhede and Shri D. M. Harish were elected as directors. With these change in the board of directors of the company, the petitioners apprehended that the Government directors may not be allowed to take part in the proceeding of the board. The petitioners were also apprehending non-compliance of the provisions of s. 408(5) of the Companies Act, 1956. Hence the present petition.

7. The principal contention of Shri Advani, learned counsel appearing for the petitioners, was that order dated 17th November, 1973, is in force until the directors appointed under that order have held office for a full term of three years and the respondent company is bound to apply under s. 408(5) of the Companies Act, 1956, for confirmation by Central Government - Company Law Board of the newly elected directors of the company at the meeting held on 30th September, 1981. The order dated 15th November, 1977, passed in the writ petition was without prejudice to the rights and contentions of the parties. The question whether the order dated 17th November, 1973, has expired or not squarely decided in the writ petition between the same parties and the decision is binding on the parties. The learned counsel further contended that the act of the court in granting stay on the operation of the order dated 17th November, 1973, and passing various other orders from time to time cannot prejudice any party to these proceedings. On the other hand, Shri Bhabha, learned counsel appearing for the respondent company, has contended that the order dated 17th November, 1973, has exhausted itself after the expiry of three years from 17th November, 1973, and, thereafter, no order is made by the appropriate authority after giving a reasonable opportunity which is necessary and after fulfilling the conditions which are precedent to the making of the order. The after, there is no question of exercise of any power contrary to the provisions of the statute. In the absence of any fresh order under s. 408(1), there is no question of approval under s. 408(5). The ad hoc board constituted under Sri Justice, Deshmukh's, order was a workable order without prejudice to the right and contentions of both the parties as expressly stated in the order and now that the annual general meeting has been held in September, 1981, and three directors, Shri Sitaram D. Morarka, Shri S. K. Wankhede and Shri D. M. Harish, have been elected. Therefore, the order under s. 408(1) has spent its force and the question of confirmation under s. 408(5) does not arise.

8. Now, in the writ petition, on behalf of the company and the petitioners therein, it was submitted that the impugned order, i.e., the order dated 17th November, 1973, was for a period of three years and of the expiry of the period of three years calculated from 17th November, 1973, the appointment of the two directors under s. 408 of the Companies Act had come to an end and, therefore, the provisions of sub-s. (5) of s. 408 were of no avail to the Company Law Board. This was in reply to the contention raised on behalf of the Union of India the Company Law Board that the Company Law Board had appointed two directors under s. 408 and that in view of the impugned order dated 17th November, 1973, having been stayed by injunction and order dated 10th January, 1974, the impugned order had not come to an end and that by reason of the order dated 15th November, 1977, the Company Law Board had appointed two directors, Shri D. D. Sathe and Shri H. Nanjundiah, and that while Shri Nanjundiah had resigned, the other director continued to be on the board of directors and in place of Shri Nanjundiah the Company Law Board had appointed Shri Khushaldas as a director. While dealing with these contentions, this is what I

had observed :

"Sub-s. (5) of s. 408 of the Companies Act, 1956, provides that no change in the board of directors made after a person is appointed or directed to hold office as a director or additional director under s. 408 shall, so long as such director or additional director holds office, have effect unless confirmed by the Central Govt. The language is clear. If any change is to be made in the board of directors after a person is appointed to hold office as a director under sub-s. (1) of section 408, and so long as such director holds office, any change in the board of directors cannot be brought about without confirmation of the Central Govt. I am not impressed by the submission made on behalf of the 8th respondent-company and the petitioner that the impugned order dated November 17, 1973, came to an end on November 16, 1976, as it was for a period of three year from the dated of the passing of that order. The injunction granted by the order dated January 10, 1974, is still in force. Even otherwise, having regard to what has been transpired in the various noticed of motion taken out on behalf to what has been company or otherwise, it is abundantly clear that the parties have proceeded on the footing that the appointment of the director under s. 408 continues, although the 6th and the 7th respondents appointed to hold office as directors under the impugned order could not participate in the meeting of the board by virtue of the injunction of this court. Nevertheless, the parties sought a variation of the undertaking given by them and brought about the appointment go new directors under s. 408(1) in place and stead of respondents Nos. 6 and 7. One of the directors, Shri D. D. Sathe, still continues to be directors appointed under s. 408(1). As regards the order director appointed under s. 408(1), the company has sought by prayer (a) of the notice of motion for appointment of a director in place of Shri H. Nanjundiah. Furthermore, in the meantime, Shri Khushaldas has been appointed as the second director. In all these circumstance, the objection now taken on behalf of the 8th respondent-company and the petitioner is an after thought."

9. Shri Advani submitted that the present matter is concluded by the above judgment. Shri Bhabha contended that the above observations are casual when there is no argument from the side of the company. These observation are not the ratio of the case. The judgment in the writ petition has nothing to do with the present petition, submitted Mr. Bhabha. The question which is before the court in the present petition was not before the court in the writ petition. Shri Bhabha referred to certain observations from the said judgment, namely, "the petition had outlived its life in view of the several interlocutory proceedings taken during the pendency of the petition", and "when the petition come up for hearing, the learned counsel for the remaining sole petitioner had advanced no argument and this would have been sufficient to give a burial to the petition" and "no attempt had been made to make out a cases for quashing or setting aside the impugned order and that the judgment of this court reported in Baldevdas R. Raheja Vs. The Union of India (UOI), , also rendered the petitioner worthless". Now, these observations do not affect the point raised and decided. They are to be read in

the context in which they appear. Individually or collectively they do not unsettle the conclusion arrived at. The contention raised in the writ petition under reference was the same as in the present petition. The controversy in the writ petition did not arise out of the blue. The order dated 15th November, 1977, was passed subject to the same contention and, therefore, it was validly raised and decided at the hearing.

10. Shri Bhabha strenuously urged that the order dated 17th November, 1973, had exhausted itself notwithstanding the decision in the writ petition. Shri Bhabha relied upon certain dates from *Baldevdas Raheja v. Union of India* [1979] 79 Bom. LR 581 to demonstrate that the order has spent its life. Shri Bhabha referred to the footnote on page 581, which says that as the impugned order had come to an end by the end of June, 1974, the petition and the order did not survive. Shri Bhabha pointed out from page 587 that the impugned order was to remain in force till 31st December, 1971, but the appointment of the two Government directors was to continue for a period of one year from 25th June, 1973, has further stated at page 591. Thus, in that case of the appointment of the Government directors came to an end by the end of June, 1974. Now, the reported judgment is of Shri Justice Rege. Against his decisions, Appeal No. 67 of 1974 was filed. The appeal was heard by Nathwani and Naik JJ. The learned judges found that the impugned order had spent its life and, therefore, the appeal did not survive. I fail to see how on the analogy or methodology of that case I can hold that the life of the order in the present case has come to an end. In the case before me, as we have seen, the order dated 17th November, 1973, could not be implemented not as the directors were restrained and the company gave an undertaking not to call a meeting of Board of Directors without the order of the court. It is not in dispute that the order dated 15th November, 1977 constituting the ad hoc board was without prejudice to the rights and contentions of the parties. The annual general meeting of the company held on 30th September, 1981, was in consequence of the order dated 15th November 1977. The purpose of allowing the election of directors was not to set at naught the appointment of two Government directors or to escape from compliance with the provisions of s. 408(5). The purpose of making workable order was not to defeat the provision of law or to put one party in position of advantage against the other. In these circumstances, the order dated 17th November, 1973, did not have the chance to become effective and operative, but became dormant or remained in cold storage. Section 408(1) provides for appointment of directors for period not exceed three years on any one occasions. Such appointees are required "to hold office as directors". The object of making the appointment of directors is to prevent the affairs of the company being conducted either in the manner which is oppressive to any member of the company or in a manner which is to the interest of the company or to public interest. If I were to accept Shri Bhabha's submission, then appointment of directors under s. 408(1) would be an empty formality and make-believe. Government directors would actually not hold office except on paper. An order under s. 408(1) can be defeated by a company

knocking at the writ (jurisdiction) door of the court, and by obtaining a stay of the implementation of the impugned order by attacking it on numerous ground which might appeal to the court for granting stay. Thus, when the period of the impugned order court for is over by efflux of time, the company can make an application to have the writ petition dismissed for want to prosecution on payment of costs of Rs. 225. In this simple manner the order can be conveniently got rid of the oppression or mismanagement sought to be prevented in the interest of the member or the company or public interest can warded off.

11. Another limb of the same contention of Shri Bhabha was that after the expiry of the order dated 17th November, 1973, on fresh order under s. 408(1) has been passed after giving the company a reasonable opportunity and, therefore, there is no question of seeking approval about the appointment of three directors elected in September, 1981. Now, in view of the earlier discussion, this part of the contention has no substance. The order dated 17th November, 1973, was sought to be quashed, but that exercise was given up at the hearing. The order has not been set aside; it has not lived its life of three years, and therefore, it is very much alive. The Government Directors are still holding office as directors and, therefore, there is no question of fresh order being made as suggested by Shri Bhabha. In my view, therefore, with the appointment of Government directors subsisting and they continue to hold office as directors, the change in the board of directors cannot have effect unless confirmed under s. 408(5).

12. In the result, I allow the petition in terms of prayers (a) and (b) with costs.

13. Shri Bhabha applies for stay of the operation of the above order in order to enable the company to file an appeal against the order. Shri Bhabha states that by order dated 22nd December, 1981, newly company Application No. 6 of 1982, the court has allowed the newly constituted board to function on certain conditions and, therefore, on the same condition the newly constituted board be continued. Shri Advani opposes the application and submits that the company has already committed several grave and serious irregularities leading to the passing of the order dated 17th November, 1973. The new board can cause immense damage and harm to the interest of the company and public interest. Shri Advani offered that if the company gives an undertaking not to call a meeting of the board till the order of the Appeal Court, he has no objection to time being granted. Shri Bhabha was not directors is the make such a statement because the chairman of the board of directors is the nominee of the Bank of Madura. Secondly, the crushing seasons is on and as such the business of the company would be affected.

14. Normally, the court is inclined to continue the stay on the same terms to enable a party to go in appeal. But, in the present case, I am not favour of following this parties. Firstly, the thirteen instances marshaled by the Company Law Board in the order dated 17th November, 1973, give a dismal picture of the acts of commission and omission committed by the company. Thought the

company had challenged the said order, it did not pursue the challenge and thereby succeeded in crippling the order. Secondly, the position of the two directors appointed by the Government is different. They are there to see that the company does not function in a manner that would harm and impair the interest of the company and the public interest. I was not told how the presence of the two Government directors and their taking part in the business of the company especially when these Government directors were on the ad hoc board. Thirdly, the reasons given that the bank nominee is the chairman of the board is not even good excuse. Fourthly, the interest of the shareholders is to be taken into account. A large number of shares have been held by the banks, insurance companies and other Government bodies. Out of a total equity shares of 6,00,000, the bank and insurance companies hold 4,56,000 shares. Thus, about 70 per cent. of the capital is contributed from public funds. Fifthly, it is evident that the company has not even suggests that it has during the course of year ratifies the said acts of commissions or omission. These are the material considerations which weigh with we in refusing the application. I, therefore, refuse the stay application.