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HIGH COURT OF DELHI AT NEW DELHI

Judgment Reserved on: 12th July, 2010

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Judgment Pronounced on: 13th September, 2010

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LPA 455/2010

YOGESHWARI KUMARI

..... Appellant

Through: Mr. Vibhu Bhakhru, Mr. A.K. Mishra and
Ms. Reshmi Rea Sinha, Advocates.

versus

THE INSTITUTE OF CHARTERED
ACCOUNTANTS OF INDIA & ANR

..... Respondents

Through: None.

CORAM:

HON'BLE THE CHIEF JUSTICE

HON'BLE MR. JUSTICE MANMOHAN

1. Whether reporters of the local papers be allowed to see the judgment? Yes
2. To be referred to the Reporter or not? Yes
3. Whether the judgment should be reported in the Digest? Yes

DIPAK MISRA, CJ

Questioning the legal acceptability and the substantiality of the order dated 19.3.2010 passed by the learned Single Judge in W.P.(C) No.2828/2008, the present intra-court appeal has been filed under Clause 10 of the Letters Patent. The appellant is the daughter of late Highness Maharana Bhagwat Singhji Mewar who was the promoter of two companies, namely, Lake Palace Hotels & Motels Pvt. Ltd. (LPHM) and Lake Shore Palace Hotels Pvt. Ltd. (LSPH). LSPH holds 49% equity shares in LPHM. The appellant is a shareholder of LSPH as well as LPHM and, therefore, claims to be interested in the affairs and management of both the said companies. The respondent no.2, a Chartered Accountant, is the auditor of LPHM.

2. The appellant – petitioner (hereinafter referred to as ‘the appellant’) filed a Company Petition No.1/1991 in the High Court of Rajasthan at Jodhpur under Sections 397 and 398 of the Companies Act, 1956 (for short ‘the 1956 Act’). On 23.11.1994, the company court appointed Maharaj Kumar Raj Singhji and Maharaj Kumar Samar Singhji as Directors of LSPH as there was a deadlock in the Board of Directors of LSPH between its Directors, namely, the appellant and her brother Sh. Arvind Singh Mewar. The said order came to be assailed before the Division Bench in three separate appeals and while the matter was pending before the Division Bench, a settlement was arrived at which was reduced to a Memorandum of Understanding dated 25.8.1999 and was signed by both of them. In terms of the settlement arrived at, all the appeals were disposed of. On 12.4.2005, the appellant filed Company Petition No.32/2005 under Sections 397 and 398 of the 1956 Act before the Company Law Board contending, inter alia, that the appointment of the respondent No.2 as the Director of the company was contrary to the circular No.14/51/62-PR of the Department of Company Affairs and sought a declaration that any business conducted at the meeting of the Board of Directors attended by the respondent No.2 was bad in law and should not be implemented.

3. The Company Law Board disposed of the petition holding that the respondent No.2 had been appointed as per the settlement which was accepted by the High Court of Rajasthan at Jodhpur and, therefore, it was obligatory on the part of the appellant to approach the High Court. The order passed by the Company Law Board came to be assailed before the High Court by filing separate appeals. She also filed two separate company applications.

4. As the facts are unfurled, in September, 2005, the appellant filed a complaint under Section 21 of the Chartered Accountants Act, 1949 (for brevity 'the CA Act') against the respondent No.2 before the Council of the Institute of Chartered Accountants of India (ICAI) alleging that the respondent No.2 had violated the code of conduct of Chartered Accountants as formulated by the ICAI as well as the circular No.14/51/62-PR of the Department of Company Affairs. It was alleged that the partnership firm of the respondent No.2 was the statutory auditor of LPHM which was a subsidiary of LSPH and, therefore, while continuing to be an auditor of LPHM, he could not have acted as a Director of LSPH. It was urged that the said continuance constituted 'professional misconduct' as specified in the First and Second Schedules to the 1956 Act. On the said complaint, comments were invited by the ICAI from the respondent No.2 and thereafter, a rejoinder was filed by the present appellant. The ICAI in its meeting dated 10.10.2007 expressed the prima facie opinion that the respondent No.2 was not guilty of professional or other misconduct.

5. The said order was called in question under Article 226 of the Constitution of India in the writ court contending, inter alia, that the respondent No.2 was disqualified in view of Section 226(4) read with Section 226(3)(b) of the 1956 Act. Reliance was placed on Section 2(30) of the 1956 Act which defines "officers" that includes a Director of a company. It was averred that an officer of a company cannot be its auditor in terms of Section 226(3) of the 1956 Act. It was set forth that as the respondent No.2 was disqualified in terms of Section 226(4) of the 1956 Act, he was disqualified from being appointed as auditor of LSPH by virtue of being its Director and further he was also disqualified from continuing as auditor of LPHM which is a subsidiary of LSPH. The order passed by the ICAI

was criticized on the ground that it has erred in forming its prima facie opinion that the respondent No.2 was not guilty of professional or other misconduct though the case is covered by Clause (11) of Part I of the First Schedule of the CA Act. The learned Single Judge, as is manifest from the order, took note of the fact that the stand of the appellant before the ICAI was that the respondent No.2 stood disqualified to continue as an auditor of LHPM in view of Clause (11) of Part I of the First Schedule of the CA Act. The learned Single Judge referred to the said provision and, after interpreting the same, came to hold that the respondent No.2 is an auditor of LHPM which is a separate corporate entity although a subsidiary of LSPH and, therefore, the respondent No.2 is not an auditor of LSPH. Since the respondent No. 2 is not an auditor of LSPH, there is no bar to be appointed as Director of LSPH in terms of the proviso to Clause (11). Being of this view, she concurred with the order passed by the ICAI. Quite apart from the above, the learned Single Judge referred to the circular of the Department of Company Affairs and thereafter came to hold that as the appointment of the respondent No.2 as the Director of LSPH is already pending consideration before the High Court of Rajasthan, the ICAI was not called upon to decide the validity of such appointment. Thus, on both the scores, the learned Single Judge accepted the order of the ICAI and did not interfere.

6. We have heard Mr.Vibhu Bhakhru, Mr. A.K. Mishra and Ms. Reshmi Rea Sinha, learned counsel for the appellant. It is submitted by the learned counsel for the appellant that the learned Single Judge has fallen into error by not unsettling the order passed by the ICAI which has failed to take note of the fact that the respondent No.2 was carrying on dual roles, a Director of a holding company and the auditor of its subsidiary company. It is urged by them that the order passed by

the learned Single Judge is totally fallacious inasmuch as he has not appreciated the scope and purport of sub-sections (3) and (4) of Section 226 of the 1956 Act and the circular No.14/51/62-PR of the Department of Company Affairs. It is their further submission that when the facts were absolutely clear, it was obligatory on the part of the learned Single Judge to dislodge the conclusion arrived at by the ICAI and not to concur with it.

7. First, we shall advert to the finding recorded by the ICAI dealing with professional misconduct. The case of the appellant, as is evincible before the ICAI, is that the respondent No.2 stood disqualified to continue as an auditor of LPHM in view of Clause (11) of Part I of the First Schedule of the CA Act. The said clause reads as under:

“(11) engages in any business or occupation other than the profession of chartered accountants unless permitted by the Council so to engage.

Provided that nothing contained herein shall disentitle a chartered accountant from being a director of a company, unless he or any of his partners is interested in such company as an auditor.”

8. The learned Single Judge, in paragraph 13, has held thus:

“13. The substantive portion of Clause 11 is attracted if a chartered accountant “engages in any business or occupation” other than “profession of chartered accountants” without the permission of the council. The appointment as director of the company, without being its employee or a whole time director drawing a salary, will not attract the phrase “engages

in any business or occupation”. Therefore, upon being appointed as a non-whole time Director of LSPH, Respondent No.2 did not commit any professional misconduct envisaged by the substantive part of Clause 11. The proviso to Clause 11 states that a chartered accountant will not be disentitled from being a director of a company, unless he or any of his partners “is interested in such company as an auditor”. The words ‘such company’ in the above proviso refers to the company in which such chartered accountant is a director. In the present case it would refer to LSPH. The proviso requires such Chartered Accountant to be interested in such company as ‘an auditor’. In other words, Respondent No.2 can be said to have committed professional misconduct in terms of the proviso to Clause 11 if he was interested in LSPH “as an auditor of LSPH” and was appointed as its director. In other words, the proviso is meant to deal with a situation where an auditor of a company is subsequently appointed as its director. As far as the present case is concerned, this is not the position. Respondent No.2 is an auditor of LPHM which is a separate corporate entity although a subsidiary of LSPH. In the considered view of this Court, since Respondent No.2 is not an auditor of LSPH, there is no bar to his being appointed as Director of LSPH in terms of the proviso to Clause 11. Consequently, the ICAI

was not in an error in coming to the prima facie conclusion that Respondent No.2 was not guilty of any professional misconduct.”

9. We have reproduced the said paragraph to understand and appreciate the approach of the learned Single Judge. On a perusal of Clause (11), it is quite vivid that the respondent No.2 was not a whole-time director of LSPH; he was not engaged in any business or occupation and, therefore, the First part of the Clause does not get attracted to his case. As far as the proviso is concerned, a Chartered Accountant is not disentitled from becoming a director of a company. The only rider is that he should not be interested in such company as an auditor. The terms which have been laid emphasis upon and correctly so are “such company” and the respondent No.2 is not the auditor of LSPH. He is the auditor of LPHM which is a separate corporate entity. Regard being had to the concept of different juris entity and keeping in view the concept of disqualification which has to be strictly construed, we are of the considered opinion that the analysis made by the learned Single Judge is absolutely impeccable.

10. The second aspect that arises for consideration is whether the circular issued by the Department of Company Affairs has its own connotation. It reads as follows:

“It is of the view of this Department that it would not be a desirable practice for a practicing Chartered Accountant ‘X’, who is connected with the managing director of Company, A or where X acts as auditor of company A, to be on the Board of Company B or to act or be employed as tax or financial adviser to company B, where company A and company B are

in the same group, because he may find it difficult to exercise
an independent judgment.”

11. On a scanning of the anatomy of the aforesaid circular, it is luculent that a practising Chartered Accountant who is connected with the management of a particular company or acts as an auditor of the company should not be employed as a tax or financial advisor of a company in the same group. Whether the respondent No.2 could have been so appointed or not regard being had to the concept of desirability is the subject matter of controversy which is pending for adjudication before the High Court of Rajasthan. It is worth noting that the disqualification in terms of Sections 226(3) and 226(4) of the 1956 Act would depend upon the decision of the Rajasthan High Court. The ICAI ought not to have ventured into the same and judicial propriety warranted that the learned Single Judge also should not have entranced into the said arena and rightly he has not done so.

12. In view of our preceding analysis, we concur with the view expressed by the learned Single Judge and the inevitable result is the dismissal of the appeal in limine which we direct.

CHIEF JUSTICE

MANMOHAN, J.

SEPTEMBER 13, 2010
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