Before Ajay Kumar Mittal & Tejinder Singh Dhindsa, JJ.

EMPLOYEE STATE INSURANCE CORPORATION—*Petitioner*

versus

M/S A.V. AUTO INDUSTRIES (P) LTD.—*Respondent*

FAO No. 448 of 1993

May 21, 2018

Employees' State Insurance Act, 1948 — S. 2(9), 2(17) & 2(22) — Employee — Managing Director of a Company falls within the meaning of employee or not — Reference to larger Bench in view of divergent views by two Division Benches — No longer res integra — Managing Director/Director of company would fall within the definition of the expression "Employee" — Employer amenable to the provisions of the ESI Act, in so far as contribution towards employees insurance — Reference answered.

Held, that the issue with regard to a Managing Director of a company falling within the meaning of "Employee" under Section 2 sub section (9) of the Act is no longer *res integra*. Such question already stands examined and adjudicated upon by the Apex Court in Employees' State Insurance Corporation v. Apex Engineering Pvt. Ltd., (1998) 1 SCC 86.

(Para 5)

Held further, that following the dictum laid down in the case of Apex Engineering Pvt. Ltd. (supra), we hold that the Managing Director/Director of the respondent company would fall within the definition of the expression "Employee" under Section 2(9) of the Act and thereby making the employer amenable to the provisions of the Act in so far as contribution towards employees insurance.

(Para 8)

G.D. Gupta, Advocate, *for the appellant.*

None for the respondent.

TEJINDER SINGH DHINDSA.J (Oral)

(1) Present appeal assailing the judgment dated 16.12.1992 passed by the Employees Insurance Court, Chandigarh has come up before us pursuant to reference made by learned Single Judge vide order dated 12.7.2017 and which reads as under:-

"In the present appeal, the issue is "as to whether the Managing Director of the Company can be included in the definition of an employee so as to force the employer to contribute towards employees' insurance".

In the impugned order, it has been held that a Managing Director is not covered under the definition of employee under the Employees State Insurance Act, 1948, by relying upon a judgment rendered by a Division Bench of this Court reported as **M/s Shibbu Metal Works, Jagadhri Vs. Regional Director, Employees' State Insurance Corporation, Chandigarh and another, 1982 Lab. I.C. 755**.

Learned counsel for the appellant inter alia has cited a Division Bench judgment of Karnataka High Court reported as**Regional Director, Employees' State Insurance Corpn Vs. M/s Margarine & Refined Oils Co. (P) Ltd, Bangalore, 1984 Lab. I.C 844**, taking a converse view.

Keeping in view the importance of the issue as well as divergent views of two Division Bench judgments, this Court feels it necessary to place the matter before Hon'ble the Chief Justice for constituting a Larger Bench.

Ordered accordingly."

(2) Facts of the present case lie in a narrow compass.

(3) Respondent is a private limited company duly registered under the Factories Act. A survey was conducted by the competent authority under the Employees State Insurance Corporation (in short the Corporation) in the month of September, 1987 and the respondent was found to have employed 18 persons for wages besides its two Directors. Directors were drawing salary @ Rs.2000/- per month w.e.f. July, 1987. Accordingly, orders dated 20.9.1988 and 21.4.1989 were issued by the Corporation making the provisions of the Employees State Insurance Corporation Act, 1948 (for short the Act) applicable upon the respondent and for claiming contribution for the period October, 1987 to July, 1988 amounting to Rs.12760/- and interest of Rs.926/-. Aggrieved of the two afore-noticed orders issued by the Corporation, respondent filed an application under Section 75 of the Act before the E.S.I Court, Chandigarh. Vide impugned judgment dated 16.12.1992 the orders dated 20.9.1988 making the respondents amenable to the provisions under the Act as also the order dated

21.4.1989 claiming contribution for the period October, 1987 to July, 1988, have been set aside. View taken by the E.S.I Court is that the work of a Limited Company is carried out by the Directors and Managing Director and therefore they would come within the definition of "Principal Employer" under Section 2(9) of the Act. Accordingly, payment made to the Directors/Managing Director cannot form the basis for assessing the contribution provided for under the Act. It was further held by the E.S.I Court that the two Directors under the respondent and who were found working and drawing salary could not be treated as "employees" under Section 2(9) of the Act.

(4) We have heard learned counsel for the appellant at length and have perused the case paper book.

(5) Section 2 sub section(9), Section 2 sub section (17) and Section 2 sub section (22) of the Act defining "Employee", "Principal Employer" and "Wages" would be relevant for the issue at hand and are reproduced hereunder:-

> "2(9).`employee' means by person employed for wages in or in connection with the work of a factory or establishment to which this Act applies and-
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> (1) Who is directly employed by the principal employer on any work of, or incidental or preliminary to or connected with the work of, the factory or establishment whether such work is done by the employee in the factory or establishment or elsewhere; or (11) who is employed by or through an immediate employer on the premises of the factory or establishment or under the supervision of the principal employer o his agent on work which is ordinarily part of the work of the factory or establishment or which is preliminary to the work carried on in or incidental to the purposes of the factory or establishment; or
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> (iii) whose services are temporarily lent or let on hire to the principal employer by the person with whom the person whose services are so lent or let on hire has entered into a contract of service; and includes any person employed for wages on any work connected with the administration of the factory or establishment or any part, purchase or branch thereof or with the purchase or branch or with the purchase of raw materials for, or the distribution or sale of the products of, the factory or establishment, or any person

engaged, as an apprentice, not being an apprentice engaged under the Apprentices Act, 1961, or under the standing orders of the establishment; but does not include-

(a) any member of the India naval, military or air forces; or

(b) any person so employed whose wages (excluding remuneration for overtime work) exceed such wages as may be prescribed by the Central Government.

Provided that an employee whose wages (excluding remuneration for overtime work) exceed such wages as may be prescribed by the Central Government at any time after (and not before) the beginning of the contribution period, shall continue to be an employee until the end of the period;

"2(17). `Principal employer' means-

(i) in a factory, the owner or occupier of the factory, and includes the managing agent of such owner or occupier, the legal representative of a deceased owner or occupier, and where a person has been named as the manager of the factory under the Factories Act, 1948, the person so named;

(ii) in any establishment under the control of any department of any Government in India, the authority appointed by such Government in this behalf or where no authority is so appointed the head of the department;

(iii) in any other establishment, any person responsible for the supervision and control of the establishment;

2(22). `wages" means all remuneration paid or payable, in cash to an employer, if the terms of the contract of employment, express or implied, were fulfilled and includes any payment to an employee in respect of any period of authorized leave, lock-out, strike which is not illegal or lay-off and other additional remuneration, if any paid at intervals not exceeding two months, but does not include-

(a) any contribution paid by the employer to any pension fund or provident fund, or under this Act;

(b) any travelling allowances or the value of any travelling concessions;

(c) any sum paid to the person employed to defray special

expenses entailed on him by the nature of his employment; or

(d) any gratuity payable on discharge;"

(6) The issue with regard to a Managing Director of a company falling within the meaning of "Employee" under Section 2 sub section (9) of the Act is no longer *res integra*. Such question already stands examined and adjudicated upon by the Apex Court in ***Employees State Insurance Corporation*** *versus* ***Apex Engineering Pvt. Ltd.***[1].

(7) In the case of ***Apex Engineering Pvt. Ltd.*** *(supra)* the E.S.I Court and a Division Bench of the Bombay High Court, Nagpur Bench held that a Managing Director employed by the respondent-company therein does not fall within the meaning of "Employee" under Section 2(9) of the Act. The High Court rather observed that the Managing Director was the Principal Employer. Overruling such view, the Apex Court held that since the Managing Director had to work under the control and supervision of the Board of Directors and to discharge his functions, he was being given remuneration of Rs.1000/- per month, the requisite conditions for applicability of the term "Employee" as defined under Section 2(9) of the Act stood satisfied. It was further held that the definition of "Principal Employer" contained in Section 2 sub section (17) of the Act would apply in a case where the Managing Director is found to be the owner or occupier of the factory. It was observed that a Managing Director by himself cannot be said to be the owner of the factory which belongs to a private limited company and the working of the factory is controlled by the entire body of Board of Directors. The Apex Court further observed that even assuming a Managing Director to be a "Principal Employer", there is nothing in the Act to indicate that the Managing Director being the "Principal Employer" cannot also be an employee as defined under Section 2(9) of the Act. In other words the Managing Director was held to have a dual capacity.

(8) Paragraphs 6, 7, 8 and 9 of the judgment rendered in ***Apex Engineering Pvt. Ltd.*** (*supra*) would be relevant and are extracted hereunder:-

"6. The controversy in the present case rotates round the interpretation of the term `employee' as defined by Section 2 Sub-section (9) of the Act. It reads as under:

"2(9).`employee' means any person employed for wages in

[1] (1998) 1 SCC, 86

or in connection with the work of a factory or establishment to which this Act applies and-

(i) Who is directly employed by the principal employer on any work of, or incidental or preliminary to or connected with the work of, the factory or establishment whether such work is done by the employee in the factory or establishment or elsewhere; or

(ii) who is employed by or through an immediate employer on the premises of the factory or establishment or under the supervision of the principal employer o his agent on work which is ordinarily part of the work of the factory or establishment or which is preliminary to the work carried on in or incidental to the purposes of the factory or establishment; or

(iii)whose services are temporarily lent or let on hire to the principal employer by the person with whom the person whose services are so lent or let on hire has entered into a contract of service; and includes any person employed for wages on any work connected with the administration of the factory or establishment or any part, purchase or branch thereof or with the purchase or branch or with the purchase of raw materials for, or the distribution or sale of the products of, the factory or establishment, or any person engaged, as an apprentice, not being an apprentice engaged under the Apprentices Act, 1961, or under the standing orders of the establishment; but does not include-

(a) any member of the India naval, military or air forces; or

(b) any person so employed whose wages (excluding remuneration for overtime work) exceed such wages as may be prescribed by the Central Government.

Provided that an employee whose wages (excluding remuneration for overtime work) exceed such wages as may be prescribed by the Central Government at any time after (and not before) the beginning of the contribution period, shall continue to be an employee until the end of the period;

A mere look at the aforesaid provisions shows that before a person can be said to be an employee the following characteristics must exist qua his service conditions- (1) He

should be employed for wages. This would pre-suppose relationship between him as employee on the one hand and the independent employer on the other;

(2) Such employment must be in connection with the work of the factory or establishment to which the Act applies;

(3) He must be directly employed by the principal employer on any work of, or incidental or preliminary to or connected with work of, the factory or establishment;

(4) In the alternative he should be employed by or through an immediate employer on the premises of factory or establishment or under supervision of principal employer or his agent;

(5) We are not concerned with clause (3) of the said definition. But the inclusive part of definition being relevant has to be noted as Condition No.5. He should be employed for wages on any work connected with the administration of the factory or establishment or any part, department or branch thereof. We are also not concerned with the exempted categories of persons in the present case and hence we need not dilate on the same.

(6) This is subject to the further condition that the wages of the person so employed excluding remuneration for overtime should not exceed such wages as prescribed by the Central Government.

The definition of `wages' is provided in Section 2 sub-section (22) of the Act. It reads as under:

"2 (22). "wages" means all remuneration paid or payable, in cash to an employer, if the terms of the contract of employment, express or implied, were fulfilled and includes any payment to an employee in respect of any period of authorized leave, lock-out, strike which is not illegal or lay off and other additional remuneration, if any paid at intervals not exceeding two months, but does not include-

(a) any contribution paid by the employer to any pension fund or provident fund, or under this Act;

(b) any travelling allowances or the value of any travelling

concessions;

(c) any sum paid to the person employed to defray special expenses entailed on him by the nature of his employment; or

(d) any gratuity payable on discharge;"

A conjoint reading of the aforesaid provisions of the Act clearly indicates that Shri Dhanwate who was one of the directors of the company was entrusted with the work of Managing Director on remuneration of Rs.12,000/- per year, that is, Rs.1000/- per month and in view of this remuneration he had to discharge his extra duties as Managing Director even apart from his function as an ordinary director. Thus it could not be gainsaid that he was receiving this remuneration under the contract of employment pursuant to the resolution of the Board of Directors and that remuneration was paid to him because he was carrying on his extra duties as Managing Director. So far as the first condition is concerned it must, therefore, he held that he was a person employed for wages and his employer was the company which is a legal entity by itself. It could not, therefore, be said that he was a self employed person or agent of the employer which would be the case of a managing partner in a partnership firm which by itself is not a legal entity. The first condition is, therefore, clearly satisfied in the present case. So far as the second condition is concerned it also cannot be denied that the duties as a Managing Director were entrusted to him in connection with the work of the establishment and for such work which he would carry out he would be entitled to the remuneration of the Managing Direct. The High court has placed strong reliance on the Articles of Association which stated the extra duties of Managing Director. But those extra duties were in connection with the work of the establishment and not dehors it and it was for these extra duties that he was to be paid the remuneration which otherwise would not have been paid to him if he had remained an ordinary director. Consequently the emphasis put by the High Court on these extra duties to be carried out by the Managing Director would not detract from the applicability of the second condition of the definition of `employee'. So far as the third

condition is concerned, by the resolution of the Board of Director he was directly employed and entrusted with the work of Managing Director. The said condition is also, therefore, satisfied. The alternative condition no. 4 would not obviously apply on the facts of the present case as it is not the case of the respondent-company that Shri Dhanwate was employed through any immediate employer other than the principal employer. So far as condition no.5 is concerned Shri Dhanwate can be said to have been employed for wages on any work connected with the administration of the establishment as his functions as Managing Director entitled hi, as noted by the High Court, to borrow money not exceeding Rs.10,00,000/- at any time with or without security as he deemed fit. He was also authorized to invest a sum not exceeding Rs.10,00,000/- in aggregate in either movable or immovable assets as may be necessary. He was further empowered to lend a sum not exceeding Rs.1,000/- without any security. These all were funds of the company which could be invested by him even the power to borrow money was also for the purpose of the company. All these activities were connected with the administration of the factory. The fifth condition was also, therefore, satisfied by him. So far as the last condition is concerned it is also not in dispute between the parties that remuneration of Rs. 12,000/- per year Rs.1000/- per month as paid to him for discharging his duties as Managing Director remained within the permissible limits of wages as prescribed by the Central Government at the relevant time for applicability of the definition of the term `employee' as per Section 2 sub- section (9) of the Act. Thus all the requisite conditions for applicability of the term `employee' as defined by the Act stood satisfied in the case of Shri Dhanwate.

7. However the Division Bench of the High Court in the impugned judgment has placed emphasis on the fact that because Shri-Dhanwate was appointed as a Managing Director with wide powers as aforesaid he could be said to be principal employer. `Principal employer' is defined by Section 2 sub-section (17) of the Act as under :

"2(17). `Principal employer' means-

(i) in a factory, the owner or occupier of the factory, and includes the managing agent of such owner or occupier, the legal representative of a deceased owner or occupier, and where a person has been named as the manager of the factory under the Factories Act, 1948, the person so named;

(ii) in any establishment under the control of any department of any Government in India, the authority appointed by such Government in this behalf or where no authority is so appointed the head of the department ;

(iii) in any other establishment, any person responsible for the supervision and control of the establishment ; The above provision would apply in a case where the Managing Director is found to be the owner or occupier of the factory. Now it is obvious that Managing Director by himself cannot be said to be the owner of the factory which belongs to the private limited company, namely, the respondent herein and the working of the factory is controlled by the entire body of Board of Directors. But the Managing Director though being one of the directors cannot be said to be the sole owner of the factory, Nor can he said to be an occupier of the factory as the does not occupy the factory only by himself. It is also not the case of the respondent that Shri Dhanwate had been named an occupier of the factory under the Factories Act, 1948. So far as the term `occupier' of the factory is concerned it is defined by Section 2 sub-section (15) of the Act to have the meaning assigned to it in the Factories Act. 1948. Dealing with the definition of the said term as found in Section 7(1) of the Factories Act Dr. A.S. Anand, J., speaking on behalf of a Bench of two learned Judges of this court in the case of J.K. Industries Ltd. & Ors. v. Chief Inspector of Factories and Boilers & Ors. [(1996) 6 SCC 665] held that to be termed as an occupier of the factory within the meaning of Section 2(n) of the Factories Act the person concerned must have ultimate control over the affairs of the factory. Dealing with the question as to who can be said to be having ultimate control over the affairs of the factory owned by a company the following pertinent observation were made:-

"21.There is a vast difference between a person having the ultimate control of the affairs of a factory and the one who

has immediate or day-to-day control over the affairs of the factory. In the case of a company, the ultimate control of the factory, where the company is the owner of the factory, always vests in the company, through its Board of Directors. The Manager or any other employee, of whatever status, can be nominated by the Board of Directors of the owner company to have immediate or day- to-day or even supervisory control over the affairs of the factory. Even where the resolution of the Board of Directors says that an officer or employee, other than one of the directors, shall have the `ultimate' control over the affairs of the factory, it would only be a camouflage or an artful circumvention because the ultimate control cannot be transferred from that of the company, to one of its employees or offices, except where there is a compete transfer, of the control of the affairs of the factory."

It cannot, therefore, be said as assumed by the High Court in the impugned judgment that Shri Dhanwate being appointed as a Managing Director could be said to be principal employer within the meaning of Section 2 sub- section (17) of the Act as he could be said to be occupier within the meaning of Section 2(15) of the Act read with Section 2 (n) of the Factories Act. As per the Articles of Association the ultimate control over his working was with the Board of Directors as a whole as the High court has noted that Shri Dhanwate was allowed to exercise all the powers exercisable by a director under the supervision and control of the Board of Directors.

8. But even assuming that the High Court was right that Shri Dhanwate could be said to be principal employer there is nothing in that Act to indicate that a Managing Director being the principal employer cannot also be an employee. It other words he can have dual capacity. So far as this aspect of the matter is concerned we can profitably refer to a decision of a Bench of three learned Judges of this Court in the case of Shri Ram Pershad (supra). In that case this Court was concerned with the question whether the Managing Director of a company can be said to be a servant of the company whose remuneration could be treated to be salary assessable to income tax. The relevant observations of this

court speaking through Jaganmohan Reddy, J., as found in paragraph 6 and 7 of the Report read as under:

"Generally it may be possible to say that the greater the amount of direct control over the person employed, the stronger the conclusion in favour of his being a servant.

Similarly the greater the degree of independence the greater the possibility of the services rendered being in the nature of principal and agent. It is not possible to lay down any precise rule of law to distinguish one kind of employment from the other. The nature of the particular business and the nature of the duties of the employee will require to be considered in each case in order to arrive at a conclusion as to whether the person employed is a servant or an agent. Though an agent as such is not a servant, a servant is generally for some purposes his master's implied agent, the extent of the agency depending upon the duties or position of the servant. It is again true that a director of a company is not a servant but an agent inasmuch as the company cannot act in its own person but has only to act through directors who qua the company have the relationship of an agent to its principal. A Managing Director may have a dual capacity. He may both be a Director as well as employee, depending upon the nature of his work and the terms of his employment. Whether or not a Managing Director is a servant of the company apart from his being a Director can only be determined by the articles of association and the terms of his employment."

In paragraph 13 of the Report relying on the Articles of Association and terms and conditions of the agreement appointing the assessee as Managing Director the following pertinent observations were made:

"Where the articles of association and terms and conditions of the agreement definitely indicate that the assessee was appointed to manage the business of the company in terms of the articles of association and within the powers prescribed therein and under the terms of the agreement he can be removed for not discharging the work diligently or if is found not be acting in the interests of the Company as Managing Director, then it can hardly be said that he is an agent of the company and not a servant. The Control which

the company exercise over the assessee need not necessarily be one which tells him what to do from day to day. Nor does supervision imply that it should be a continuous exercise of the power to oversee or superintend the work to be done. The control and supervision is exercised and is exercisable in terms of the articles of association by the Board of Directors and the company in its general meeting. The fact that power which is given to the Managing Director emanates from the articles, of association which prescribes the limits of the exercise of that power and that the powers of the assessee have to be exercised within the terms and limitations prescribed thereunder of the Directors in indicative of his being employed as a servant of the company. Hence remuneration payable to the assessee would be salary."

We have already seen the powers and duties of Managing Director as entrusted to Shri Dhanwate as per the Articles Association. They clearly indicate that he had to work under the control and supervision of the Board of Directors and to discharge his function to earn his remuneration of Rs.1000/- per month by working as Managing Director and by discharging extra duties as entrusted to him.

The aforesaid decision of this Court clearly rules that the Managing Director while acting as such can have dual capacity both as Managing Director on the one hand and as servant or employees of the company on the other. The Division Bench is the impugned judgment with respect was in error in bypassing the ratio of the aforesaid decision of this Court by observing that it was a judgment rendered under the Income Tax Act and, therefore, it had no bearing on the scheme of the present Act. We also find that the Division Bench was equally in error when it placed reliance for its decision on the judgment of this court in the case of Regional Director Employees State Insurance Corporation Trichur v. Ramanuja Match Industries (supra). In the said decision a Bench of two learned Judges of this Court held that a partner of a firm receiving salary is not an employee within the meaning of Section 2 sub-section (9) of the Act. Ranganath Misra, J. (as the then was), speaking for this court held that the partners cannot be held employees of the

partnership firm. A partnership firm is not a legal entity and in a partnership firm each partner acts as an agent of the other. The position of a partner qua the firm is thus not that of a master and a servant or employer and employee which concept involved an element of subordination and not that of equality. The partnership business belongs to the partners and each one of them is an owner thereof. In common parlance the status of a partner qua the firm is thus different from employees working under the firm. It may be that a partner is being paid some remuneration for any special attention which he devoted but that would not involve any change of status and bring him within the definition of employee."

(9) Following the dictum laid down in the case of ***Apex Engineering Pvt. Ltd.*** (*supra*), we hold that the Managing Director/Director of the respondent company would fall within the definition of the expression "Employee" under Section 2(9) of the Act and thereby making the employer amenable to the provisions of the Act in so far as contribution towards employees insurance.

(10) The reference is answered accordingly.

(11) In view of the above, the impugned judgment dated 16.12.1992 passed by the E.S.I. Court, Chandigarh, is set aside. As a sequel thereto the orders dated 20.9.1988 and 21.4.1989 passed by the appellant Corporation making the provisions of the Act applicable upon the respondent w.e.f. 1.10.1987 as also claiming contribution for the period w.e.f. October, 1987 to July, 1988 towards employees insurance, stand revived.

(12) Appeal is allowed in the aforesaid terms.

V. Suri