ARBITRABILITY OF OPPRESSION, MISMANAGEMENT AND OTHER PREJUDICE CLAIMS IN INDIA

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ABSTRACT

The famed Cyrus Mistry case[1] scandal, which surfaced recently, has sparked discussion about corporate governance and the powers of the NCLT and NCLAT. The SC clarified that the main objective of the Tribunal is to bring an end to the matters complained by providing a solution and not put an end to the company itself along with forsaking the interests of other stakeholders, as stated in the legislation itself "*with a view to bringing to an end the matters complained of*."[2] Transparency is a key necessity to corporate governance, the absence of which leads to Oppression and Mismanagement in the Company. To protect the interests of shareholders, Chapter XVI has been incorporated in the Companies Act,2013 which lays down the law relating to Oppression and Mismanagement. The 2013 Act, also conducts prejudice to any member or prejudice to the public interest, or prejudice to the interest of the company, which are all added along with oppression. However, neither term, Oppression or Mismanagement, have been defined in the Companies Act 2013, thus the scope relies entirely on judicial interpretation. The term oppression is made out as where the conduct of the authority is harsh, burdensome, and wrongful and the action is against probity and good conduct. [3]The circumstances and effects giving rise to mismanagement have been specified under section 241(1)(b) of the Companies Act, 2013. For the petition under this section to succeed, it must be established that the affairs of the company are being conducted in a manner prejudicial to the interest of the company or public interest, or that, or by any change in the manner and control over the company and it is likely that the affairs of the company will be conducted in that manner.[4] Under the new law the test of 'winding-up on just and equitable grounds' is applicable to mismanagement under the Companies Act, 2013.[5] This was earlier a test considered for oppression which was not an essential test. The NCLT has powers under Sec 242 of the Act to pass any required order to end such prejudice. The tribunal has been

[1] Tata Consultancy Services Ltd. v. Cyrus Investments (P) Ltd., (2021) 9 SCC 449
[2] Sec 242(1) of the Companies Act, 2013
[3] Needle Industries Ltd. v Needle Industries Newey Holding Ltd. and Ors (1981) 3SC 212
[4] Section 241(1)(b) of the Companies Act, 2013
[5] Section 242 of the Companies Act, 2013

given wide powers which have been discussed in various noteworthy cases such as in the *Bennet Coleman v. Union of India*[6]. It is essential to note here that the powers under these provisions are not affected by the existence of an arbitration clause. This article will expand on this scope of arbitration and such prejudice claims.

BODY

Not all disputes can be arbitrated. [7] As stated by Russell, only the disputes affecting civil rights may be referred to arbitration. [8] In order to understand the arbitrability of such prejudice claims it is necessary to examine the nature of the disputes concerning oppression and mismanagement. Adjudication of certain categories of proceedings[9] is reserved by the legislative exclusively for the public as a matter of public policy.[10] Petitions under sec 241 have an essence of action *in rem*[11]. Due to its nature of affecting the rights of the third parties, any dispute involving right *in rem* cannot be referred to arbitration. [12] Hence, this very factor acts as an estoppel against the arbitration of such petitions. Even if the petition involves both- right *in rem* and right *in personam*, there cannot be a severance of the involved rights.[13] Additionally, the rights under Sec 242 are statutory in nature, while the rights pertaining to the parties to the arbitration are contractual. Thus, the presence of an arbitration clause in the Article of Association of a Company cannot restrict a petition being filed u/s 241 to the NCLT. Further, an agreement for arbitration, legally validated by Section 7 of the Arbitration Act is merely an agreement under the Indian Contract Act, and hence very well comes under the purview of overriding the effect of Section 6 in the Companies Act, 2013. Consequently, the arbitration agreement, in absence of any statutory authority gets ousted by section 6, and hence a petition u/s 241 of the Companies Act prevails over any contractual agreement for arbitration.[14]

[6] Bennet Coleman and Co. v Union of India (1977) 47 Comp Cas 92 (Bom)
[7] G England and I McKenna Arbitrability Restrictions in Action, Relations Industrielles/Industrial Relations, Vol. 47, No. 2 (Spring 1992), pp. 279-99; Arbitrability' of Labor Disputes, Virginia Law Review, Vol. 47, No. 7 (November 1961), pp. 1182-208
[8] D Sutton and J Gill Russell on Arbitration (22nd ed. Sweet & Maxwell Publications), p. 28.
[9] CB Manzoni Arbitration in the Public Sector, The Labor Lawyer, Vol. 1, No.2 (Spring 1985), pp. 454-73.
[10] RD Horton Arbitration, Arbitrators, and the Public Interest, Industrial and Labor Relations Review, Vol. 31, No. 1 (October 1977), pp. 76-7.
[11] Rakesh Malhotra v. Rajinder Kumar Malhotra & Ors.: MANU/MH/1309/2014.
[12] Booze Allen and Hamilton Inc. v. SBI Home Finance and Others: 2011 (5) SCALE 147., Chiranjilal Shrilal Goenka v.Jasjit Singh and Ors.: 1993 (2) SCC 507.
[13] Periyakaruppiah vs P.VG. Raju (Dead) & Others: Application Nos. 4214 & 4215 of 2009, Sukanya Holdings Pvt. Ltd v.Jayesh H. Pandya: (2003) 5 SCC 531.
[14]Act to override memorandum, articles, etc.— Save as otherwise expressly provided in this Act— (a) the provisions of this Act shall have effect notwithstanding anything to the contrary contained in the memorandum or articles of a company, or in any agreement executed by it, or in any resolution passed by the company in general meeting or by its Board of Directors, whether the same be registered, executed or passed, as the case may be, before or after the commencement of this Act; and (b) any provision contained in the memorandum,

Besides, a plain reading of section 2(3) of the Arbitration Act makes it clear that the provisions of the Act are in addition to and not in derogation of the provisions of any other law in force.[15] The Supreme Court confirmed the position of law with respect to the wavering of rights and held that any statutory rights vested in public interests cannot be waived even through voluntary executed contracts.[16] Accentuating the above view, the Bombay HC stated that vide Sec 242 NCLT, was empowered to substitute the management, and regulate the affairs of the company, among other things. Since the power to provide such relief is enjoyed exclusively by the NLCT, no arbitration agreement can empower the arbitral tribunal to grant such reliefs.[17] Essentially, an arbitrator would have no jurisdiction to pass a winding-up order on the ground that it is just and equitable as it falls within the exclusive domain of the NCLT under Sec 271(e) of the Companies Act, 2013.[18]

It is indispensable to mention here that in certain situations, a party may "dress up" the dispute as falling within the ambit of Sections 241 and 242 of the Companies Act, 2013. This is often done in order to include reliefs that can only be granted through the NCLT. The NCLT accepted that with such "dressed up" petitions driven with mala fide intentions to evade an arbitration clause, the matter may be referred to arbitration. It is the duty of the NCLT to investigate the real substance of a suit and allow arbitration in required cases. [19] At times the Court has held that the reference to Arbitration was mandatory in consonance with a prior agreement for the same. [20]The reference to arbitration needs to be subjectively decided based on the facts of the case. In the *Shin-Etsu Chemical Company case*, SC held that if on a *prima facie* determination, the court finds that the arbitration agreement is not null and void, inoperative, or incapable of performance, the parties would be referred to arbitration.[21] In many oppression, mismanagement, and prejudice claims, legal strangers to the cause of action are added as parties to defeat the arbitration agreement. For instance, in some cases, the directors of the company, who are not parties to the arbitration agreement, are added as parties to the oppression, mismanagement, and prejudice petition solely to avoid reference of the dispute to

articles, agreement or resolution shall, to the extent to which it is repugnant to the provisions of this Act, become or be void, as the case may be.

[15] Section 2(3) of Arbitration & Conciliation Act 1996: 'This Part shall not affect any other law for the time being in force by virtue of which certain disputes may not be submitted to arbitration.'

[16] All India Power Engineer Federation v. Sasan Power Ltd. (2017) 1 SCC 487

[17] Rakesh Malhotra v. Rajinder Malhotra (2015) 127 CLA 140

[18] Dhananjay Mishra v. Dynatron Services Private Limited Company Appeal (AT) No. 389/2018

[19] Malhotra *supra* note 11

[20] Naveen Kedia v. Chennai Power Generation Ltd 1999 95 CompCas 640 CLB. Pinaki Das Gupta v. Maadhyam Advertising P. Ltd (2002) 4 Comp LJ 318 (CLB). Gurnir Singh Gill & Anr. v. Saz International P Ltd 1987 62 ITR 197 Delhi. Escorts Finance Ltd. v. G.R. Solvents & Allied Industries Ltd (1999) 96 Comp Cas 323.

[21] Shin-Etsu Chemical Co. Ltd. (1) v. Vindhya Telelinks Ltd., (2009) 14 SCC 24

arbitration. [22]In order to check such despicable methods adopted by some of the parties, courts and judicial authorities in India have adopted the 'necessary parties' test. As per this test, the courts and judicial authorities examine whether (i) an effective order can be passed in oppression, mismanagement, and prejudice petition; and (ii) a complete and final determination be made without the presence of the party which is not a party to the arbitration agreement. Unless a party to the oppression, mismanagement, and prejudice dispute (not a party to the arbitration agreement) satisfies the 'necessary parties' test, the dispute will be referred to arbitration. [23]However, the legality of the "necessary parties" test has been deemed to be debatable. If there is no commonality between the parties to the arbitration agreement, the petition need not be referred to arbitration.

In order to initiate a petition, the concerned shareholder(s) must be eligible u/s 244 of the Companies Act, 2013. [24]If they fail to satisfy the mentioned conditions, a petition cannot be filed to NLCT. However, although the Companies Act is silent on dispute resolution mechanisms for those not fulfilling the eligibility criteria, it has not debarred them from approaching any other authority. The question arises if, in this scenario, a petition concerning oppression and mismanagement could be fit for arbitration. However, on careful analysis of the situation, it becomes obvious that the arbitrator, again, will not be able to grant relief like those specified under section 402 of the Companies Act. Hence, the problem with the arbitration, as already discussed, persists in this scenario as well, as it again turns out to be illusory in nature. So, in case of non-eligibility, it is recommended for the shareholder(s) to file a suit in a civil court and tend to bring a civil action against the company. Civil court, by exercising its inherent powers guaranteed u/s 151 of Code of Civil Procedure, 1908,41 and by the authority u/s 9 of CPC,[25] is capable of granting reliefs on terms of those specified u/s 402,

[22] Shreyas Jayasimha & Rohan Tigadi, Arbitrability of Oppression, Mismanagement and Prejudice Claims in India: Need for Re-Think? 11 NUJS L. REV. 547 (2018).
[23] *See generally*, Sidharth Gupta v. Getit Infoservices (P) Ltd., 2016 SCC OnLine CLB 10.
[24] Right to apply under section 241.— (1) The following members of a company shall have the right to apply under section 241, namely:— (a) in the case of a company having a share capital, not less than one hundred members of the company or not less than one-tenth of the total number of its members, whichever is less, or any member or members holding not less than one-tenth of the issued share capital of the company, subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares; (b) in the case of a company not having a share capital, not less than one-fifth of the total number of its members: Provided that the Tribunal may, on an application made to it in this behalf, waive all or any of the requirements specified in clause (a) or clause (b) so as to enable the members to apply under section 241. Explanation. —For the purposes of this sub-section, where any share or shares are held by two or more persons jointly, they shall be counted only as one member. (2) Where any members of a company are entitled to make an application under subsection (1), any one or more of them having obtained the consent in writing of the rest, may make the application on behalf and for the benefit of all of them.
[25] Section 15 1 of Code of Civil Procedure, 1908:'Nothing in this Code shall be deemed to limit or otherwise affect the inherent power of the court to make such orders as maybe necessary for the ends of justice or to

and hence is a more appropriate and suitable forum. Thus, arbitrability of the petitions involving oppression and mismanagement fails in such cases too.

On the other hand, Singapore and UK courts seem to take a view that disputes relating to oppression are *per se* arbitrable. According to Singaporean and UK law, the fact that an arbitral tribunal is not capable of granting certain reliefs granted by courts in oppression claims is not a relevant criterion for determining the arbitrability of oppression claims. Further, the lack of commonality between the parties to the oppression petition and the parties to the arbitration agreement; and the subject matter of the oppression not being fully covered by the arbitration agreement between the parties, are not relevant factors for staying in court proceedings and referring the parties to the arbitration. [26]The stark differences between the structural designs of the Indian Arbitration Act, Singapore Arbitration Act, and UK Arbitration Act in terms of stay of proceedings and the permit of bifurcation of claims and proceedings, may account for the reasoning behind why their principles relating to the arbitrability of such matters is not applicable to the Indian legal context.

CONCLUSION

Hence, it is concluded that Arbitration can lead to speedy remedy but it does not deem to be efficient in cases of Oppression and Mismanagement and other such prejudice claims. The issue of arbitrability of oppression, mismanagement, and prejudice claims in India arises during the pre-arbitral stages in India i.e., the majority shareholders in control of the company resist such claims filed by minority shareholders by seeking reference of the underlying dispute to arbitration u/s 8 and u/s 45 of the Indian Arbitration Act, 1996.[27] In pursuance with the aforementioned findings, of the Remedies Test, Bifurcation of Claims Test, The Necessary Parties Test, and the Totality Test, the article concludes with the notion that the issue of arbitrability of such prejudice petitions relating to Oppression and Mismanagement u/s 241 of the Companies Act,2013 is against the arbitrator, and preferably titled in favor of the NCLT (when eligibility is fulfilled u/s 244) or a civil court (if eligibility is unfulfilled u/s 244). The possibility of taking such claims and solving them through the means of International Arbitration Centres is plausible but not always feasible. Reverting to the *Cyrus Mistry*[28] case,

prevent abuse of the process of the court. Section 9 of Code of Civil Procedure, 1908: 'Courts to try all civil suits unless barred - The Courts shall (subject to the provisions herein contained) have jurisdiction to try all Suits of a civil nature excepting suits of which their cognizance is either expressly or impliedly barred'

[26] Tomolugen Holdings Ltd and Another v. Silica Investors Limited and Other Appeals, [2015] SGCA 57; See also L Capital Jones Ltd and Anotherv. Maniach Private Limited, [2017] SGCA 03.

[27] Jayasimha & Tigadi *supra* note 17

[28] Mistry *supra* note 1

SC stated that the Tribunal should always keep in mind the purpose for which remedies are made available under Sections 241 and 242 of the Companies Act, 2013 before granting relief or issuing directions, which must be in line with the several changes in the law relating to oppression and mismanagement as well as address the issue which brought up such petitions.