Dispute Resolution Hotline

April 08, 2016

OPPRESSION & MISMANAGEMENT CASE DISMISSED IN FAVOR OF SINGAPORE SEATED ARBITRATION

- Mere violation of contractual terms does not automatically fall within the ambit of oppression and mismanagement
- If acts alleged are de hors any malice or malfeasance then such acts would not take the color of oppression.

INTRODUCTION

The Company Law Board, New Delhi Bench ("**CLB**") in *Sidharth Gupta & Ors. Vs. M/s. Getit Infoservices Pvt. Ltd. & Ors.*[1] dismissed the petition for oppression and mismanagement under Section 397 & 398 ("**Petition**") of the Companies Act, 1956 ("**Act**") and referred the parties to arbitration under the SIAC Rules seated in Singapore. The CLB noted that its jurisdiction under Section 397 and 398 of the Act can be invoked even if governed by arbitration if the oppression and/or mismanagement is seen on the facts of the case. However jurisdiction under Section 397 and 398 of the Act cannot be invoked for mere violation of the articles of the company or provisions of the law without involvement of any malice or malfeasance.

FACTS IN BRIEF

The Petition was filed by the promoters ("**Petitioners**") of Getit Infoservices Pvt. Ltd. ("**Company**") who had entered into a Shareholder's Agreement ("**SSHA**") with Respondent No. 2 in the Petition ("**R2**") allowing them to purchase a 50.1% shareholding in the company. The terms of the SSHA were made a part of the Articles of Association ("**AOA**") of the Company. The SSHA provided for an arbitration clause as per which disputes between the parties were to be referred to the Singapore International Arbitration Center ("**SIAC**").

Post the initial investment, R2 made further rounds of investment into the company to enable the company to meet its loan liability and other funding requirements. This initially raised R2's shareholding in the company to 76%. Pursuant to the investment made by R2 in September 2013, the Company allotted equity shares to R2 at the rate of Rs. 53.22 per share based on the valuation report of M/s. Sanjeev Sapra and Associates ("**Valuer**").

The Petitioners filed the oppression and mismanagement action alleging that the price of the shares were highly undervalued, and that the respondents had therefore acted prejudicially to the interests of the Company by allotting a substantially higher number of shares to R2 at the cost of diluting the Petitioners' shareholding in the Company. The Petitioners further alleged fraud based on the grounds that (i) the Company had not given adequate notice before holding the Company's Extra Ordinary General Meeting ("**EOGM**") to increase the authorized share capital and (ii) the valuation report of the valuer was unquestionably accepted by the members of the board during the Board meeting.

The Petitioners therefore, inter alia, sought reliefs in relation to (i) allotment of shares of the Company, (ii) composition of directors and (iii) regulation of the affairs of the company. They argued that since such reliefs could only be granted under Section 402 and 403 of the Act, such reliefs could not be referred to arbitration. The Company thereafter filed a Company Application ("**Application**") in the Petition to refer the dispute to arbitration as provided for in the arbitration clause in the SSHA.

ISSUE BEFORE THE CLB

Whether the subject matter of the Petition falls within the ambit of jurisdiction under Sections 397, 398 read with 402 and 403 of the Act respectively or within the ambit of the arbitration clause constituted in the SSHA arrived at between the parties.

JUDGMENT & ANALYSIS

The CLB first decided whether the dispute in question amounted to oppression and mismanagement. It observed that the only issues raised were that the notices for the EOGM and Board meeting were not given adequately in advance, the valuation report did not reflect the fair market value and that the person preparing the report was not in accordance with the Articles of the Company.

The CLB observed that though the meeting was held with a shorter notice, it was not clarified how this prejudiced the interests of the members or the company. It was noted that the company was in need of the funds and that an equal offer was made to the Petitioners to subscribe to the issue. It was also noted that R2 had offered to allot shares to the Petitioners on a loan basis. While the meeting was held at a shorter notice, the rights issue was kept open for thirty days. Thus, the CLB observed that no case appropriation of the entire share allotment had been made by the Petitioners. With regard to the valuation report, the CLB noted that another valuation report had been obtained which reflected a similar valuation. Thus, the CLB found there to be no case for oppression or mismanagement.

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The CLB further analyzed whether the dispute was adequately covered by the arbitration agreement within the SSHA. In this regard, the first issue was regarding the parties to the arbitration agreement not being the same as the parties to the petition before CLB. CLB noted that the persons not party to the arbitration agreement are the nominee directors of R2 itself and are in fact persons representing the cause of R2. Thus such an objection was unsustainable. The CLB thereafter noted the various articles which were said to be breached had percolated from the SSHA itself.

In *Rakesh Malhotra vs Rajinder Kumar Malhotra*[2] ("**Malhotra Judgment**") the Bombay High Court had discussed the CLB's plenary and expansive powers along with the issue of petitions merely 'dressed up'as oppression and mismanagement cases in order to oust an arbitration clause. The Court observed that in assessing whether the petition has been properly brought before the CLB, the same must be read as a whole including the reliefs sought therein. In such an assessment, if it is found that there are certain reliefs that fall within Section 402 of the Act, then the petition cannot be dismissed merely on the grounds that there exists an arbitration agreement. (Please click here to access our hotline on the Malhotra Judgment).

The CLB in this case however, found the reliefs being sought for to be very much covered by the arbitration agreement and that even if the case of the Petitioners was assumed to be correct, it only brought up the issue of contractual violations, which could very well be settled through arbitration. CLB therefore held that mere violation of articles of association or provisions of law does not amount to oppression unless such action or conduct is laced with malfeasance or malice.

In the case of *Vikram Bakshi & Anr. V. Mc Donald's India Pvt. Ltd.*[3] ("**Mc Donald's judgment**"), the Delhi High Court observed that since allegations of mismanagement and oppression were pending before the CLB for more than a year, including an ad interim order already passed restraining the defendants from proceeding with a change in the shareholding pattern of the company, the arbitration agreement is rendered inoperative. It also observed that the petition pending before the CLB would have certain overlapping disputes with respect to the disputes sought to be referred to arbitration. Considering the fact that in such a scenario, there was bound to be conflicting decisions, it restrained the defendants from pursuing arbitration while the matter remained pending before the CLB. (Please click here to access our hotline on the Mc Donald's Judgment).

It appears that the CLB seems to have taken a practical approach in this case and has gone beyond mere technicalities to ensure that the smooth functioning of the Company is not unnecessarily interfered with. The CLB went as far as to observe that the Petitioners were attempting to couch a mere contractual dispute into an issue of oppression and mismanagement merely to stall the Company. Such a decision should therefore discourage parties from filing oppression and mismanagement actions merely with a view to stall the functioning of the company and avoid alternative dispute resolution mechanisms. It may however be noted that the order of the Company Law Board has been appealed before the Hon'ble High Court of Delhi and the matter is currently pending.

– Siddharth Ratho, Ashish Kabra & Vyapak Desai
You can direct your queries or comments to the authors

[1] CA 128/ C – II/ 2014 in CP 64 (ND) 2014
[2] Company Appeal (L) Nos. 10, 11, 12, 13, 16, 17, 18, and 19 of 2013 and Company Appeal No. 15, 16, 17, 18, 23 and 24 of 2013
[3] IA Nos. 6207/2014 and C.S(OS) No. 962/2014 (Delhi High Court)

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