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ANALYSIS OF POLICY FOR PREVENTION OF MINORITY SHAREHOLDERS AND OPERATION MISMANAGEMENT

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ABSTRACT

In the process of decision making in any part of organization is depend on the system which is called voting. And decision is taken based on the majority. That's full and final. But every decision making have its own method and preceding which we have to follow it. And decision taken by it is accepted by everyone. Now in the corporate culture decision is made in board meeting by the voting of shareholders. Every shareholders have right to vote in general meetings depends on their holdings and types of share. In appreciation of holding there are greater part shareholders holding immense measure of offer contrast with minority shareholders. The said procedure is disappointed when there is a contention of feeling between the greater part and minority shareholders whereby, majority shareholders take choices, not in light of a legitimate concern for the organization but rather to take into account their impulses and likes gravely prejudicing the privileges of minority shareholders. The Companies Act, 2013 thought of the answer for handle the issues which are normally looked by the minority shareholders. However, there is no clarity of act toward define who is the minority shareholder. So that objective of paper is that to analysis the impact of after amendment of minority shareholder in Companies Act 2013.

KEYWORDS: *Minority Shareholder, Operation and Mismanagement, Companies Act 2013.*

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Introduction

Democratic decisions are made in line with the majority decision and the same rule was also applicable in the Companies cases also. As per the Companies Law, shareholders who hold the majority of share, rule the organization. The choice taken by the majority shareholders was official on the minority. At present, one of the significant destinations of Indian corporate routine is the strengthening of each shareholder of the organization, including the minority shareholders (Varma, 1997). The minority shareholders in principle have measure up to rights simply like the majority shareholders however regularly minority shareholders wind up in a position where they are compelled to move their offers and leave the organization or their rights are frequently abused by the majority shareholders.

The point must be to strike a harmony between the powerful control of the organization and the interests of the little individual shareholders.[1] This vote based rule is regularly portrayed as the 'majority rule'. This is otherwise called the rule in Foss v. Harbottle. However, this rule is liable to specific confinements and the Companies Act provides for statutory reliefs in instances of persecution and bungle. Section 397 of the Companies Act, 1956 (Section 241 of the Companies Act, 2013) gives a right to the members of a company who comply with the conditions or section 399 (Section 244 of the Companies Act, 2013) to apply to the court for relief under section 402 (section 242 of the Companies Act, 2013) or such other reliefs as may be suitable in the circumstances of the case, if the affairs of the company are being conducted in a manner oppressive to any member or members including any one or more of those applying.[2]

Various provisions have been presented in the Companies Act 2013 to basically overcome any issues towards security and welfare of the minority shareholders under Companies Act 1956. The idea of

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[1] N.A. Bastin, "Minority Protection in Company Law" (1968) JBL 320.
[2] Amit Kumar Pathak And Siddarth Singh, Scope of Sections 397 and 398 of Companies act, 1956: A Critical Analysis, (2012) 1 CompLJ 133 (Journal).

class action is included the Companies Act 2013 however in 1956 Act there was no such idea in the Act. According to Section 245 of the Companies Act, 2013 class action can be organized against the Company just as the examiners of the Company. This class action must be documented by the minority shareholders. Purpose of the Sec 245 isn't just to enable the minority shareholder yet in addition the investors.

Rule in FOSS v. Harbottle[1]

For this situation the action was by two shareholders in an organization against the chiefs accusing them of concerting and affecting various deceitful and illicit transactions whereby the property of the organization was twisted and squandered, and supplicating that the respondents may be declared to make great to the organization the misfortunes (Wedderburn, K. 1957). The action was rejected in appreciation of those transactions which a majority of the shareholders had the ability to affirm. Quickly, the feeling of the court was this: "The lead with which the litigants are charged is damage not to the offended party's exclusively; it is damage to the entire partnership. In such cases the rule is that the organization should sue in its very own name and in its corporate character. It's anything but a the usual result for any individual individuals from an enterprise in this manner to expect to themselves the directly of suing for the sake of the partnership. In law the partnership and the total of individuals from the organization are not a similar thing for purposes this way." In some respects shareholders of public companies are in a better position in that they are able to realize some of their investment if need be by simply selling their shares if the majority misbehave. Of course the selling shareholder may suffer a loss due to the bad publicity of the majority's unfair conduct towards the minority which may affect the company's profitability and in turn its share value.[2]

Exceptions to 'The Rule in FOSS v. harbottle'

They are cases where the rule in *Foss v. Harbottle*simply has no application.[3]i.e., the minority shareholders may bring an action to protect their interest:

- **Ultra Virus and Illegal Acts**

The rule in Foss v. Harbottle does not have any significant bearing where the act whined of is ultra vires the organization, since not by any means a consistent vote of the shareholders can approve such an act.

- **Breach of Fiduciary Duties**

A derivative action possibly brought against directors and promoters who have been guilty of a breach of their fiduciary duties to the company, on the off chance that they can keep the organization from suing them in its very own name since they control a majority of the votes at a general gathering, or in light of the fact that they are generally ready to keep a general gathering from settling that the organization will sue them. Thus, derivative actions have been permitted against directors who were in control of the company for misappropriating the company's property.[4] In *Satya Charan Lal v. Rameshwar Pd. Bajoria*[5], it was observed that when a director is in breach of fiduciary duty, every shareholder may be regarded as an authorized organ to bring the action.

- **Fraud or Oppression against Minority**

The fraud or oppression need not amount to a tort at common law, but it must involve an unconscionable use of the majority's power resulting, or likely to result, either in financial loss or in unfair or discriminatory treatment of the minority, and it must certainly be more serious than the failure of the majority to act in the interest of the company as a whole, which will induce the court to annul a resolution altering the company's memorandum or articles.[6]

- **In adequate Notice of a resolution passed at a meeting of members**

It has been held in many cases that if an insufficiently informative notice is given of a resolution to be planned at a general meeting, any member who does not attend the meeting, or who votes against the resolution, may bring a representative action to restrain the company and its directors from carrying out the resolution.[7]

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1 Supra Note 3

2 HICKS & GOO's, *Cases and Materials on Company Law,* 425 (Oxford University Press, 7th Edn., 2011)

3 HICKS & GOO's, *Cases and Materials on Company Law,* 428 (Oxford University Press, 7th Edn., 2011)

4 Spokes v. Grosvenor Hotel Co. [1897] 2 QB 124.

5 [1950] S.C.R. 394.

6 Pennington's Company Law, 5th Edition, Page 734.

7 Tiessen v. Henderson [1899] 1 Ch. 861, Mac Connell v. E. Prill& Co. Ltd [1916] 2 Ch.57.

- **Qualified Majority**

Where the act or the articles require a qualified (or special) majority for passing of a resolution, 'the rule in *Foss v. Harbottle* cannot be invoked to override these requirements. If this were not so, provisions requiring qualified majorities would be valueless because a bare majority could always confirm a special resolution passed irregularly. The action brought by a shareholder to complain of an irregularity in the passing of a special resolution would seem to be a personal one.

- **Statutory Exceptions**

The Companies Act, 2013, vide certain specific provisions, extends protection to the minority shareholders by conferring certain rights on them: (i) Variation of class rights provided in section 48, (ii) Request for investigation under section 213, (iii) Scheme of compromise and arrangement in section 230, (iv) Oppression and mismanagement, (v) Rights of dissentient shareholders under take-over bids in section 235, and (vi) Class action under section 245.

Oppression and the Minority Shareholders

- **What is Oppression?**

The expression 'Oppression' has not been defined by the Companies Act, 2013. In general oppression means causing damage or injury by unjust exercise of power or unrestricted authority, specially with unjust motives (Afterman, A. B. 1969). In the context of a company it may mean depriving of one or more shareholders of their legitimate expectations or other unfair treatment by the controlling shareholder(s).[1] Justice Wanchooquoted with endorsement in Shanti Prasad Jain v. Kalinga Tubes Ltd. the entry from the Scottish instance of Elder v. Elder and Watson Ltd.[2] , on section 210 of the English Act, which is like section 397 (presently section 241 of Companies Act, 2013) of the Companies Act, 1956. For this situation it was extravagantly clarified that:

  - The oppression of which a candidate whines must identify with the way in which the undertakings of the organization concerned are being led; and the lead griped of must be.
  - In proceedings under section 397 of Companies Act, 1956 (now section 241 of Companies Act, 2013) it is not legality or illegality of action complained of is of primary importance but whether the act(s) is oppressive is of paramount importance."

- **Relief in Case of Oppression**

There is no meaning of 'oppression' in the Companies Act however for statutory insurance against 'oppression', the court must be in a situation to infer that the undertakings of an organization have been led constantly in a way that is oppressive to a portion of its individuals. In this manner it might be noticed that:

  - Relief might be allowed under this section just if there are persistent acts with respect to the majority shareholders which are oppressive to the minority. The direct should be difficult, cruel and unjust. Minor detached acts don't add up to oppression.
  - However, if there should arise an occurrence of Deepak C. Shriram v. General Sales Ltd. , it was held that even a solitary and confined act can constitutea genuine reason for grievance of oppression under section 397 (presently 241 of Companies Act, 2013) if its impact is for all time and persistently cruel or oppressive to any part. Accordingly where further share have been issued falsely by the respondents so as to increase outright control of the organization, it can't be rejected on the ground of being single and detached act.

- **Application to Tribunal in Case of Oppression**
  - that the undertakings of the organization are being directed in a way biased or onerous to a part or a few individuals or in a way which is biased to the open intrigue or in a way biased to the interests of the organization;
  - a material change has occurred in the administration or control of the organization, regardless of whether by an adjustment in the Board of directors, or supervisor, or in the responsibility for organization's share or its participation, or in some other way at all, and that by reason of such change, all things considered, the undertakings of the organization will be led in a way biased to its interests or its individuals or any class of individuals.

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[1] http:// www.businessdictionary.com/definition/oppression.html#ixzz3YD9guli8

[2] (1952) SC 49

If an oppression of this kind is established, the Tribunal will, “with a view to bringing to an end the matters complained of, make such an order as it thinks fit”.[1] Before this section was enacted the only effective remedy against oppression was a winding up order under the just and equitable cause. But this remedy was often worse than the disease. And now the tribunal has been given the powers to impose upon the parties whatever solution it considers just and equitable in the circumstances (Yarrow, G. 1985). Thus, instead of forcing a sound business concern to winding up, an effort is made to salvage it.

Right to Apply

The requisite number of members who must sign the application is given in section 241 of the Companies Act, 2013. The requirement varies with the fact as to whether the company has a share capital or not and is as below:-

- In case of a company having a share capital, the application must be signed by :
  - At least one hundered members, or
  - By at least 1/10th of the total number of its members, whichever is less.

In the alternative, a valid application may be made by any member(s) holding not less than 1/10th of the issued share capital of the company.

The application to be valid, the applicant or applicants must have paid all calls and other sums due on their shares. Joint holders of shares shall be counted as one member. The CLB (now tribunal) in *KishanKhariwal v. Ganganagar Industries Ltd.*[2] has held that if a person’s shareholding which was 10% or more gets below 10% by issue of further shares, such person can maintain the petition provided he has challenged further issue in his petition.

- In case of a company not having share capital, application will be valid if signed by at least 1/5th of the total number of members of the company.[3]

The Delhi High Court has held in *Suresh Kumar Sanghi v. Supreme Motors Ltd.*[4] that the provisions of section 397 of the Companies Act, 1956 (Section 241 of the Companies Act, 2013) would be applicable only in cases of oppression by majority shareholders on the minority shareholders.

In *Needle Industries Ltd. v. Needle Industry Newey (India) Holding Ltd.*[5], the Supreme Court did not uphold the allegation of oppression as valid. The leader of the Indian 40 percent holding was the chief executive and the managing director of the company. The company was further required to reduce its foreign holding to 40 percent. At this stage the English and Indian blocks developed a difference. The English block wanted that the 20 percent reduction of their holding should be allotted to one of the Indian companies in which they had substantial interest. A meeting of the company’s Board of directors, on the contrary, adopted the policy of issuing new shares to the existing members, which the English company would not be able to subscribe and thereby its holding would be reduced to 40 percent. Under the resolution 16 days’ time had to be given to the members to take their proportion. The letter offering its proportion to the holding company was sent only 4 days before the last date and it received the letter after the date for exercising the option had already expired. Similarly, the notice of the meeting of directors for completing the allotment was sent to them with so short a gap of time that they received it in England only on the day on which the meeting was being held in India. Neither it was able to exercise the option of buying its block of rights shares nor was it able to attend the crucial meeting of the board. Its block of shares was allotted to Indian shareholders.

The holding company complained of oppression on these facts. But the court was not convinced that there was any such thing as a continuous policy of oppression. The ultimate purpose of the scheme was Indianisation to the extent of 60 percent. This could be achieved either by buying the excess holding of the English company or by increasing the Indian shareholding. The latter course was adopted in the interests of the company as it would make available to the company extra capital. The fact that proper notice was not given, no doubt, deprived the English company of its opportunity of participating in the rights issue (Thompson, R. 1999). But the facts were such that even if proper notice was given, the English company could neither have subscribed for its proportion nor renounced it to

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1 Section 242 of the Companies Act, 2013.
2 [2004] 50 SCL 567.
3 Section 244 of the Companies Act, 2013.
4 (1984) 3 Comp LJ 9 (Del).
5 AIR 1981 SC 1298 : [1981] 3 SC 333.

anyone else. There was no right in the company's articles in favour of any member enabling him to renounce his rights shares in favour of others. In the case of a private company there simply cannot be the right of renouncing rights shares in favour of nominees because that would make it impossible for the company to restrict the number of members. The real loss suffered by the holding company was the loss in terms of the market value of the shares which fell. The market value of the shares was much higher than their nominal value. The loss of the holding company was the "unjust enrichment" of those whom the block of rights shares was allotted which, but for the policy restriction, belonged to that company. The Supreme Court accordingly held that the Indian allottees of those shares must compensate the holding company to the extent to which the market value was in excess of the nominal value.

Who Cannot Apply

The following cannot apply for relief under section 241 of the Companies Act, 2013

- A member/(s) whose calls are in arrears[1].
- A holder of a letter of allotment of a party paid share
- A holder of a share warrant
- A holder of a share certificate to bearer
- A transferee of shares who has not lodged the shares for transfer to the company.
- Shareholders of a holding company cannot file petition against a subsidiary of the holding company.[2]

Matters Relating to Minority Shareholders' Rights

Reconstruction and Amalgamation

Regarding minority shareholder rights at the time of reconstruction and amalgamation of companies, Companies Act, 1956 under Section 395 states that exchange of share or any class of share of an organization (transferor organization) to another organization (transferee organization), must be approved by holders of atleast nine-tenths (9/10) in value of the share whose exchange is involved inside four months after the offer has been made by the transferee organization. Thus note that assent of (90%) shareholders is required, which is alluded to as majority. The section further provides that inside two months after the slip by of the previously mentioned four months, the transferee organization will give a notice to any contradicting shareholders communicating its craving to secure their share. shareholder who has not consented to the plan or contract and any shareholder who has fizzled or would not exchange his share to the transferee organization as per the plan or contract.

To counter these shortcomings, Companies Act, 2013 has provided for *Power to acquire shares of shareholders dissenting from scheme or contract approved by majority*[3] and *Purchase of Minority Shareholding*[4]. Section 235 of Companies Act, 2013 is relating to Section 395 of Companies Act, 1956 and provides that exchange of offers or any class of share in the transferor organization to transferee organization requires approval by the holders of at the very least nine-tenths (9/10) in value of the share whose exchange is involved and further the transferee organization may, give notice to any contradicting shareholder that it wants to secure his share. Companies Act, 2013, in addition to minor improvements to certain provisions of Companies Act, 1956 has also introduced new provisions affecting the reconstruction and amalgamation procedures. These, *inter alia*, include:

- Companies Act, 2013 vide Section 235(4) in appreciation of 'Contradicting Shareholders' provides that the entirety received by the transferor organization must be paid into independent financial balance inside the predefined timeframe as against the provision referenced in Section 395(4)of Companies Act, 1956 which needed lucidity on this viewpoint;
- According to Companies Act, 2013, Section 236 (1) and (2), the Acquirer on getting to be enlisted holder of (90%) or a greater amount of issued value share capital will offer minority shareholder for purchasing value shares at the decided value;
- Section 236 (3) of Companies Act, 2013 has provided the minority with an option to make an offer to the majority shareholders to buy its shares; and

1 Section 244 (1)(a) of the Companies Act, 2013 .
2 Herbertson Ltd. v. Kishore Rajaram Chhabria [1999] 21 SCL 99 (CLB).
3 Section 235 of the Companies Act, 2013.
4 Section 236 of the Companies Act, 2013.

- Section 236 (5) of Companies Act, 2013 requires the transferor company to act as a transfer agent for making payments to minority shareholders.

Minority Upgraded

Besides other provisions, the Companies Act, 2013 has sought to empower the minority shareholders in corporate decision making also. It requires listed companies to appoint directors elected by small shareholders, i.e. shareholders holding share of ostensible value of not in excess of twenty thousand rupees . The Draft Companies Rules expounds the provision in such manner and provides that a recorded organization may either suo-moto or upon the notice of at the very least five hundred (500) or one-tenth (1/10) of the all out number of little shareholders, whichever is less, choose a little shareholders' executive from among the little shareholders.[1] Here, it is important to note that small shareholders are different from the minority shareholders as small shareholders are ascertained according to their individual shareholding which should be less than twenty thousand rupees; whereas minority shareholders/shareholding is collectively ascertained and regarded as having non-controlling stake in the company. The Draft Companies Rules further accommodates the technique for selection of a little shareholder director and the data and assertion to be given in such manner. To shield the enthusiasm of the little shareholder and to keep up the autonomous basic leadership by such directors, the Draft Companies Rules gives that such director will not be obligated to resign by revolution and will have residency of three years. Be that as it may, the little shareholder director won't be qualified for reappointment.

While engaging the minority/little shareholders in the basic leadership process, the Companies Act, 2013 undertakings to assist its present arrangements to shield the enthusiasm of minority shareholders through arrangement of free directors. The 'Code of Independent Directors' given as per Section 149(8) in Schedule IV of the Companies Act 2013, gives that free directors will inter alia move in the direction of advancing the certainty of minority shareholders.

Highlights of Kotak Committee Report

SEBI shaped an advisory group on corporate administration in June 2017 with the end goal of upgrading the models of corporate administration of recorded elements in India.

The terms of reference of the panel were to make proposals to SEBI on the accompanying issues:

- Ensuring autonomy in soul of Independent Directors and their active investment in working of the organization;
- Improving shields and revelations relating to Related Party Transactions;
- Issues in bookkeeping and examining practices by recorded companies;
- Improving viability of Board Evaluation practices;
- Disclosure and straightforwardness related issues, assuming any;
- Any other issue, as the Committee regards fit relating to corporate administration in India.

The protection of minority shareholders is also included in the domain of various references mentioned above. The committee in its report[2] also discussed various provisions, the existing situation of the protection of minority shareholders and gave its recommendations. The following were the recommendations of the committee in the interest of the minority shareholders:

- **Quorum for Board Meetings**

The Committee is of the opinion that in view of the increased obligations of the boards of listed entities, a higher quorum may be required vis-à-vis other companies. The Committee also believes that in the interest of all stakeholders, especially minority shareholders, the presence of at least one independent director is required for every board meeting.

- **The institution of Independent Directors**

With the institution of the Independent Directors being the backbone of the governance of a company, it is imperative that there are sufficient Independent Directors on a board to ensure safeguarding of interest of all stakeholders, especially minority shareholders. To improve governance, it

[1] Clause 11.5 of Chapter XI of The Draft Companies Rules.
[2] The committee submitted its report on October 5, 2017 and the same was issued by Securities and Exchange Board of India. Report available at <http://www.nfcg.in/KOTAKCOMMITTEREPORT.pdf>.

is recommended that every listed entity, irrespective of whether the Chairperson is executive or non-executive, may be required to have at least half its total number of directors as Independent Directors. However, given that this may require significant changes to the composition of the boards, the Committee felt that appropriate transition time should be provided for effecting such change. In this regard, the Committee recommends that this be applicable to top 500 listed companies by market capitalization by April 1, 2019 and to the rest of listed companies by April 1, 2020.

- **Exclusive Meeting of Independent Directors**

Independent Directors represent the interests of all stakeholders, especially minority shareholders. At the first instance, the Independent Directors are appointed by the shareholders. In the same spirit, the Committee recommends that any appointment to fill a casual vacancy of office of any Independent Director should also be approved by the shareholders at the next general meeting.

- **Quorum for Committee Meetings**

Independent Directors bring an unbiased perspective to the proceedings of committee/board meetings, which improve the quality of governance and decision making. In order to protect the interest of all stakeholders, especially minority shareholders, it is recommended that for meetings of each such committee of the board, the composition of which statutorily requires at least one Independent Directors, the presence of at least one Independent Directors may be made mandatory for attaining quorum for such meetings.

Conclusion

In modern law, giving the courts the power by the statute to control the exercise of discretion by persons or institutions on grounds of 'unfairness' is hardly novel. Though the scope of practical application of provisions in English and Indian laws is very similar, yet there exist certain inherent differences between the two. The priorities with respect to the company law policy of the systems are certainly different. Firstly, the Central Governemnt has a permeating role in the proceedings before the Tribunal. In England, no such mechanism is contemplated. Secondly, there is no mention of a public interest in the English provisions, but finds a definite place in the Indian context. The perceptual distinction would be organization as an instrument for monetary improvement from one perspective and as machines of social welfare on the other. An exercise in careful control between the requirement for giving benefit based freedom and counteracting mischief to the social welfare is required in India. A board of trustees headed by Mr. Jamshed J. Irani made for Corporate Reforms mentioned the accompanying objective facts concerning minority privileges of which many have been fused in the Companies Act, 2013:

- Upon cautious examination of the arrangements of the Companies Act, 2013 it tends to be discovered that administrative purpose in Companies Act, 2013 is to protect the minority enthusiasm for an increasingly extensive way. Notwithstanding, the arrangements of Companies Act, 2013 not just requires legitimate usage after tending to the present lacunas yet additionally requires imparting trust in the minority shareholders regarding the institutional and administrative component which guarantees that enthusiasm of minority shareholders will be given due thought. This double methodology towards requirement of minority rights will just ensure legitimate organization of the corporate activities. By and by, Ministry of Corporate Affairs' exertion in arrangement of a system, which tries to enable minority shareholders, is exemplary.
- In this way the new Companies Act, 2013 from various perspectives guarantee that the privileges of the minority shareholders are secured in each conceivable way. The stake held by them in an organization isn't in any way subservient to the majority and it is the obligation of the law to shield their interests from any evil activity of the last mentioned.

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