Dispute Resolution Hotline

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BOMBAY HIGH COURTS RULES ON ARBITRABILITY OF OPPRESSION AND MIS-MANAGEMENT ISSUES

- Bombay High Court holds that oppression and mis-management claims fall outside the purview of an arbitration proceeding.
- Petitions filed before Company Law Board if malafide, vexatious or oppressive and is merely a dressed up to avoid arbitration, then it can be referred to arbitration.
- Company Law Board is bound by the orders of a foreign court if ruling on the same issue and not entitled to take its own view, subject to complying with principles under Section 13 of Civil Procedure Code.

The Bombay High Court recently in the case of *Rakesh Malhotra* v. *Rajinder Kumar Malhotra*[1] held that maintainability of oppression and mis-management claims by minority shareholders as referred under Section 241 read with Section 242 of the Companies Act, 2013 or Sections 397 and 398 read with Section 402 of the Companies Act, 1956 ("**Companies Act**"), would not be affected by the existence of an arbitration clause. Allegations of oppression and mis-management fall outside the purview of an arbitration agreement, a *sine qua non* for an arbitration proceeding.

FACTS

Supremax Group, world's second largest manufacturer of razor blades and allied products, was run by Rajindra Kumar Malhotra ("**RKM/Respondent**") and his family members. Major portion of the business was controlled by RKM and his wife along with his younger son Rajiv and his wife Kunika, who had small shareholdings therein. There are and were several companies in this group, both in India as well as overseas. Following a restructuring in 2008 all the assets, business and plants that belonged to Indian companies were transferred to a newly incorporated company under the control of Rakesh Malhotra ("**Appellant**"), RKM's elder son. However, RKM along with his wife and younger son continued to hold some equity in those Indian companies.

During the course of restructuring, a Subscription and Shareholding Deed ("**SSD**"), Supplementary Deed along with other business agreements, were executed that gave Appellant the sole authority to represent the Respondent in all transactions. The Appellant also became the sole bank account operating authority and deployed funds received by Indian companies held by RKM to, *inter-alia*, guarantee bank loans and other facilities to the newly formed company under his control. The SSD contained an arbitration clause providing for resolution of disputes in Geneva under the rules of London Court of International Arbitration. By virtue of the restructuring, all the directors of the RKM-held Indian companies became employees of the entities controlled and held by the Appellant. Subsequently, no information was divulged to RKM related to funds deployed or other liabilities incurred due to Appellant's actions.

RKM along with others, to prevent diversion of funds, filed several company petitions before Company Law Board ("**CLB**") at different locations u/s 397, 398 read with S. 402 of the Companies Act, alleging oppression and mis-management, seeking wide orders of removal and appointment of directors, setting aside the re-structuring. During the same period, Appellant obtained an ex-parte anti-suit injunction from the Commercial Court of Queen's Bench Division of the Royal Courts of Justice ("**UK Court**") restraining Respondent from proceedings before CLB, which was subsequently over-turned as proceedings before CLB related to post-restructuring dealings and transactions. The Appellant thereafter filed applications before CLB seeking orders to refer the dispute to arbitration under S. 45 of the Arbitration & Conciliation Act, 1996 ("**Act**").

The application was dismissed and CLB held that no such reference could be made to arbitration in case of allegations of oppression and mis-management. CLB also appointed an independent Observer-cum-Facilitator on the Board. The present dispute arose from a group of appeals filed against the CLB order on the issue whether disputes arising out of SSD should be referred to arbitration.

ISSUES

The primary issue before the Bombay High Court ("**Bombay HC**") was whether disputes under Section 397 and 398 read with S. 402 of the Companies Act can ever be referred to arbitration. While deciding the same, the Bombay HC also looked into the aspect whether decisions of foreign court ("**UK Commercial Court**") was binding on CLB.

CONTENTIONS

Appellant's Arguments

The Appellant contended that there should not be any blanket embargo on reference to arbitration. If a dispute falls within the realm of an arbitration agreement, then such reference must be made regardless of the kind of relief arbitral tribunal can provide. The Appellant relying on Section 45 of the Act submitted that it makes no reference to

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relief or power but only to the dispute.

The Appellant also submitted that CLB is not bound by the decision of UK Commercial Court as it was contrary to the Supreme Court decision in *Chloro Controls India (P.) Ltd. v. Severn Trent Water Purification Inc.*[2] which held that in case of several agreements constituting a composite transaction, the court may for an effective and complete implementation make reference to arbitration even of the disputes existing between signatory or non-signatory parties. Therefore, order passed by CLB that current disputes are not covered by arbitration is not conclusive under S. 13(c) of CPC.

Further with respect to applicability of Sections 397 and 398 and their allied sections it was submitted that they do not confer exclusive jurisdiction on CLB to exclude the jurisdiction of the Civil Court. It is therefore wholly illogical to say that an action seeking an alternate remedy under Sections 397 and 398 by the same party under same agreement cannot be referred to arbitration, although, had that very party come to a civil court, the reference to arbitration would have been inevitable.

Respondent's Arguments

The Respondent submitted that any dispute invoking the powers under Section 402 of the Companies Act is inherently incapable of being referred to a private dispute resolution tribunal. There need not be an express ouster or bar. However, the test must be in relation to the source of power and not on how the relief is casted or split up. Equally it is not possible to refer some reliefs to an arbitral resolution while retaining others for a determination by the CLB.

The Respondent relied on several past decisions[3] and submitted that issue arises whether the source itself permits any such reference to a private dispute resolution. Jurisdiction of CLB under Sections 397 and 398 is statutory and therefore it cannot be ousted by an arbitration clause. The Respondent contended that disputes before CLB were outside the purview of arbitration clause in the SSD as it involved different parties, therefore the ruling of the UK Court was conclusive and binding, thus the Appellant could not re-agitate the same issue in another forum, having lost in the one of his own choice.

JUDGMENT AND ANALYSIS

The Bombay HC dismissed the appeal dealing with the following issues.

A. Case of Oppression and Mismanagement not to be referred to arbitration

The Bombay HC while examining the issue of oppression and mis-management before an arbitral tribunal, analysed all the provisions of the Companies Act in relation to oppression and mis-management, held they are not capable of being referred to arbitration, having regard to the nature and scope of the power invoked.

S. 8 and 45 of the Act use the expression "*a judicial authority, when seized of an action in a matter in respect of which the parties have made an agreement*" (S. 45), and "*a judicial authority before which an action is brought in a matter which is the subject of an arbitration agreement*" (S. 8). The operative word here appears to be "matter". Therefore, the "*matter*" must be the one in respect of which there is an arbitration agreement in order to be referred to arbitration. In an oppression and mismanagement "action" before the CLB, the "matter" invokes CLB's statutory powers under those sections including S. 402 and not exercisable by a civil court. The civil courts are vested with the power to entertain an action in oppression and mis-management, however, not the same as vested with CLB under S. 402 of the Companies Act. Therefore, disputes in oppression and mis-management cases are those such that demand the exercise by the CLB of its wide powers under S. 402 and not those that can be exercised by a civil court, certainly not by an arbitral forum.

Several precedents were considered and were referred to analyse powers of CLB in an oppression and mis-management cases and whether it was in the nature of an action *in rem*. The Bombay HC relying on past decisions including ***Haryana Telecom Ltd. v. Sterlite Industries (India) Ltd.***[4], which held that though petition for winding up is a matter *in rem*, no agreement between parties can vest an arbitral panel with such power of winding up. Similarly, no arbitration agreement can vest an arbitral tribunal with the powers to grant the kind of reliefs against oppression and mismanagement that the CLB might provide. The Bombay HC held that if CLB's plenary and expansive powers are properly invoked and petitions are not mala fide, oppressive, vexatious or an attempt at dressing up to evade an arbitral clause, then a narrowly tailored arbitral proceeding or merely the existence of an arbitration agreement is not sufficient to capture the broad and far reaching reliefs that can likely be sought by parties in such cases. CLB is vested with the powers to refer disputes to arbitration if petition is mischievous, vexatious and malafide.

B. Decision of a foreign court is binding on the CLB

The Bombay HC held that the decision given by UK court, on the issue whether petition before CLB was covered by the aforementioned arbitration clause, was not covered by any of the exceptions to S. 13 of Code of Civil Procedure, 1908 ("**CPC**"). Therefore, it bound the CLB, and the CLB was not, as it held, "*free to take its own view*". That being so, there is no question of any reference being made to arbitration. Conclusive and binding nature of judgment is decided based on the issues before it. The Bombay HC held that UK Court decision was on the same issues which were before the CLB and therefore the reasoning given by the CLB for not being bound by the orders of the foreign court were untenable.

CONCLUSION

This ruling marks an important step in clarifying the issues related to overlap of arbitration proceedings and maintainability of oppression and mis-management claims before CLB. The judgment has thrown light upon the limitations of an arbitral tribunal to entertain cases of oppression and mis-management. However, at the same time it has clarified that CLB is bound by the orders made by a foreign court if ruled on the same issue. Thus, from the commercial perspective, parties should be mindful at the stage of drafting their arbitration clause and depending on the relief sought, should approach the correct forum as both are mutually exclusive.

– Payel Chatterjee & Vyapak Desai

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[1] [2015] 53 taxmann.com 135 (Bombay)

[2] [2013] 1 SCC 641

[3] Surendra Kumar Dhawan v. R. Vir, [1977] 47 Comp Cas 276 (Delhi); See also Manavendra Chitnis v. Leela Chitnis Studios P. Ltd., 1985 (58) Comp Cas 113

[4] [1999] 2 SCL 156 (SC)