Prevention of Oppression and Mismanagement

The essence of the matter seems to be that the conduct complained of should at the lowest level involve a visible departure from the standard of fair dealing and violation of the conditions of fair play on which every shareholder, who entrusts his money to a company is entitled to rely.

Justice Wanchoo In Shanti Prasad Jain v. Kalinga Tubes
AIR 1965 SC 1535, citing Lord Cooper in Elder v. Elder & Watson

***Kalinga Tubes* v. *Shanti Prasad Jain* [1965, Orissa HC]**

“ We shall first take up the case under Section 397 of the Act and proceed on the assumption that a case has been made out to wind up the company on just and equitable grounds. This is a new provision which came for the first time in the Indian Companies Act, 1913, as Section 153. That section was based on Section 210 of the English Companies Act, 1948, which was introduced therein for the first time. The purpose of introducing Section 210 in the English Companies Act was to give an alternative remedy to winding up in case of mismanagement or oppression. The law always provided for winding up, in case it was just and equitable to wind up a company. However, it was being felt for some time that though it might be just and equitable in view of the manner in which the affairs of a company were conducted to wind it up, it was not fair that the company should always be wound up for that reason, particularly when it was otherwise solvent. That is why Section 210 was introduced in the English Act to provide an alternative remedy where it was felt that, though a case had been made out on the ground of just and equitable cause to wind up a company, it was not in the interest of the shareholders that the company should be wound up and that it would be better if the company was allowed to continue under such directions as the court may consider proper to give. That is the genesis of the introduction of Section 153C in the 1913 Act and Section 397 in the Act.

These observations from the four cases referred to above apply to Section 397 also which is almost in the same words as Section 210 of the English Act, and the question in each case is whether the conduct of the affairs of a company by the majority shareholders was oppressive to the minority shareholders and that depends upon the facts proved in a particular case. As has already been indicated, it is not enough to show that there is just and equitable cause for winding up the company, though that must be shown as preliminary to the application of Section 397, It must further be shown that the conduct of the majority shareholders was oppressive to the minority as members and this requires that events have to be considered not in isolation but as a part of a consecutive story. There must be continuous acts on the part of the majority shareholders, continuing up to the date of petition, showing that the affairs of the company were being conducted in a manner oppressive to some part of the members. The conduct must be burdensome, harsh and wrongful and mere lack of confidence between the majority shareholders and the minority shareholders would not be enough unless the lack of confidence springs from oppression of a minority by a majority in the management of the company's affairs, and such oppression must involve at least an element of lack of probity or fair dealing to a member in the matter of his proprietary rights as a shareholder. It is in the

light of these principles that we have to consider the facts in this case with reference to Section 397.

The fact that the affairs of the Company were managed with holding of shares in equal proportion amongst the 3 groups for a period of about 4 years by itself cannot create a right in favour of the petitioner and his group to claim that it must continue in the same manner contrary to the terms of the Articles of Association even when the Company becomes public. Such a claim would also be contrary to the provisions of Section 81 of the Act which lays down that General body of the share-holders can direct fresh issue of shares in a different manner. It would also not be compatible with dynamic concept of industrial expansion. for instance, the expansion scheme would require large capital in crores and any one of the groups may not be in a position to subscribe its proportionate shares as any one or both of the residual groups can do. The balance is bound to be disturbed and the equilibrium lost even if the affairs of the Company would be conducted wholly bona fide."

Oppression of Majority

- ***Sindhri Iron Foundry, Re*** **[Calcutta HC, 1963]**

  "It is true that in the case of Companies functioning normally under the doctrine of majority rule, it is the oppressed minority who comes to Court for relief. The majority seldom, if ever, has the occasion to come to Court for relief because it can always have things done in its own way. But there may be cases, as in the instant case, when the real majority is rendered ineffective by the wrongful acts and man oeuvres of a minority. The situation may be such, as in the instant case, that remedy cannot be obtained by the operation of the machinery in the domestic forum. Can it be said that even in such cases the Court is powerless to intervene and provide a remedy in exercise of its jurisdiction under **section 397 and section 398**? I think not. This Court has not only the jurisdiction, but it is the duty of the Court to intervene, if it finds the situation to be such as it is, in this case.... The sections nowhere prescribe that the applications under the two sections can be made only by a minority group. Nor do they prescribe that a majority group can under no circumstances come to Court for redress, whatever may be the nature and extent of the oppressive acts of rival group and whatever may be the extent of the injury suffered by the company as a result of the activities of such a group. Both the sections are in Chapter VI of the Act and the heading of the Chapter is "prevention of oppression and mismanagement". Thereafter the sections give, to any members of a Company the right to come to Court for the acts complained of. Section 399 of the Act lays down conditions to ensure that the application is made or supported by a minimum number. But while the minimum has been fixed by section 399 there is nothing about the maximum...

  .. The Legislature intended by those sections that the application must be moved or supported by a minimum number, which in the opinion of the Legislature is substantial for the purpose of an application under sections 397 and 398. It never intended to impose any limit on the maximum. And I see no reason why in an appropriate case, if the court is satisfied about acts of oppression or mismanagement, relief cannot be granted even if the

application is made by a majority, who have been rendered completely ineffective by the wrongful and ultra vires acts of a minority group. If the court finds that the company's interest is being seriously prejudiced by the activities of one or other group of shareholders, that two different registered offices at two different addresses have been set up, that two rival Boards are holding meetings, that the Company's business property and assets have passed into the hands of unauthorised persons who have taken wrongful possession and who claim to be shareholders and Directors, that the bank accounts of the company have been practically frozen, there is no reason why the Court should not make appropriate orders to put an end to such matters."

- ***Dr. V. Sebastian and Ors. v. City Hospital P. Ltd. and Ors* [Kerala HC, 1985]**

It is true that ss. 397 and 398 are intended primarily to protect the minority interests. In ordinary cases, the majority will be able to protect itself by controlling the directors at general body meetings. But, where the majority is prevented from doing so, despite the clear indication in the articles that majority rule based on the right to demand poll should operate as a correcting influence, the majority becomes an artificial minority entitled to claim protection under ss. 397 and 398. When the directors with the majority backing, oppress the minority and misconduct the affairs of a company, occasion arises for interference by the courts. But, when the directors, with only minority support, seek to stifle the majority by taking advantage of some defect or error, I think such a situation can also be remedied in a like manner. The Calcutta High Court has held in Sinduri Iron Foundry (P.) Ltd., In re [1964] 34 Comp Cas 510, that such a remedy is available to the majority when it is rendered ineffective by the wrongful acts of a minority. (The decision was confirmed in appeal-See Ramashankar Prosad v. Sindri Iron Foundry (P.) Ltd., AIR 1966 Cal 512).

- ***J.P. Srivastava & Sons (P) Ltd. and Ors.* v. *Gwalior Sugar Co. Ltd. and Ors.,*** (2005) 1 SCC 172

The Supreme Court noted that any member/members of a company may apply under Sections 397 and 398 of the Act to the CLB complaining of mis-management or oppression "provided such member or members have the requisite shareholding as prescribed under Section 399 to do so".