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IS THERE A BALANCE BETWEEN MINORITY RIGHTS AND MAJORITY GOVERNANCE UNDER THE COMPANIES ACT OF 2013?

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INTRODUCTION

For a long time, the corporate world has been experiencing shareholder disputes. This issue affects people all throughout the world, not only in India. A fundamental component of sound corporate governance is corporate democracy, since the term "governance" in public law appears to have political connotations.

One of the democratic pillars of contemporary company law is that all businesses function on the principle of majority rule. This principle is based on the fundamental idea that directors are the representatives selected by the business's members and, as such, are empowered to manage all day-to-day operations. According to the majority rule, the majority of shareholders have the authority to decide at general meetings how the firm is administered. A majority of members make the final decision in such a meeting.

The Rule of majority has been followed in many countries including India. Since it is deemed to be just, reasonable, and legitimate, this guideline is typically followed when making judgments pertaining to the administration and operation of the corporate world. It is beneficial to the nation's economy and legal system in addition to the firm in many ways. It allows for collective action on the part of enterprises. In the leading case of *Mac Dougall v. Gardiner* (1875), 1 Ch. D¹. it is said that it saves the court's time and people money by preventing infructuous actions of minority group. This rule fosters business success, and the more prosperous businesses are, the stronger the national economy becomes.

¹ *Mac Dougall v. Gardiner* (1875), 1 Ch. D

However, the rights and privileges of minority shareholders are limited, which frequently results in the violation of those rights over the history of the company because their voice was previously ignored under the pretext that they had insufficient or no effective say. There are a number of allegations made by the minority group on the rule of majority. The company Act of 2013 has given the minorities the rights to claim relief for oppression and mismanagement, but the question is the effectiveness of these rights.

In this research paper we will firstly understand the Rule of majority, secondly we will discuss the effectiveness of the rights and privileges of the minority stakeholder in the company in India. Lastly we will discuss the landmark judgements briefly.

METHODOLOGY

The methodology used to completely study the “Is there a balance between minority rights and majority governance under the companies act of 2013?” is philosophical in character and is based upon primary as well as secondary sources.

primary information such as Supreme Court rulings and legislative regulations.

secondary data such as news stories, journals, and other like pieces.

MAJORITY SHAREHOLDER

A shareholder that owns and controls the majority of a corporation's stock or has the ability to cast the majority of votes in a general meeting of the company is considered to be a majority shareholder. As such, they have control over all significant decisions pertaining to the management and appointment of directors, among other things. It has an impact on minority shareholders' rights since they are essentially denied a voice in how the business is governed.

A majority shareholder of a corporation is defined as an individual or group that holds more than 50% of its outstanding shares. In particular, this gives the majority shareholder complete control over the company's activities, including choosing the company's board of directors. While not all majority shareholders participate in the day-to-day activities of the business, the majority do.

The majority of the shareholders are often the founders of the company and so they generally have more power than other shareholders combined.

RULE OF MAJORITY SHAREHOLDER

Rule of majority shareholder means the day to day activities of the company are governed by these shareholders. They hold the upper hand in the company and have a dominating position towards the minority shareholders.

This rule was first established in the case of *Foss v. Harbottle*² a ruling in England when the judge decided that the majority would always have the final say and that the court would not get involved. Two shareholders, Foss and Turton, have filed an allegation in the firm's general meeting that the directors had misappropriated and defrauded the company of its assets. In a public meeting, however, the majority of shareholders decided not to pursue legal action against the directors, asserting that they had no liability whatsoever. Thus, the plaintiff filed a lawsuit in a court of law, claiming that the defendants had deceived the firm in multiple ways, including by selling the company its land at a price well in excess of its true value and by fraudulently mortgaging the property. They begged that the defendant would reimburse the company for all of its losses.

However, the court dismissed the lawsuit on four reasons, one of which being the majority rule. The court decided that whatever the directors did, the company's majority group had already corrected it in a public meeting, so the court would not become involved in this matter. The court noted the rationale that there is no mechanism to take a matter to court if someone claims that anything is being done illegally or irregularly and the majority is free to act lawfully or regularly. The majority rule is beneficial in preventing infructuous litigation, the court decided. Afterwards, several cases adopted this logic.

In *MacDougall v. Gardiner*,³ Mellish LJ noted that the majority rule really helps to prevent pointless litigation when he stated:

“If the thing complained of is a thing which in substance the majority of the company are entitled to do, or if something has been done irregularly which the majority of the company are entitled to do regularly ... there can be no use in having litigation about it, the ultimate end of which is only that a meeting has to be called, and then ultimately the majority gets its wishes.”

² (1843) 67 ER 189.

³ *MacDougall v. Gardiner* (1875) 1 CHD 13 CA. See also *Burland v. Earle* (1902) AC 83, P.C

The court also ruled that minority groups must abide by the "Majority Rule," which states that choices made by the majority are obligatory on them.

The Bhajekar v. Shinkar⁴ case in India is the first to apply the proper majority rule in a legal dispute involving the BOD's appointment of certain individuals as managing agents. The BOD passes a resolution in favour of the appointment, but some directors disagree, suing to claim the appointment was improper. The lawsuit was dismissed by the court, however, on the grounds that it was not maintainable because the majority group had approved it in a general meeting, despite its irregularities. Though the Bombay High Court noted that "officious interference by the court in such matters would paralyze the working of all joint-stock companies" in Parshuram v. Tata Industrial Bank, Ltd., the court had already acknowledged the non-interference principle in somewhat.

Occasionally, the majority shareholder would adopt immoral actions that violated the rights of minorities with the support of majority rule. Therefore, with the growth of the corporate world, various exceptions to this rule arose for the protection of minority rights because the rigorous application of majority rule might occasionally prove to be harsh and unfair for minority shareholders.⁵

MINORITY SHAREHOLDERS

All shareholders should be treated equally within the corporate governance framework. What minority can be is the most essential question that comes to mind when we talk about minority shareholders. It is a concept of comparative law whose meanings are based only on the idea of majority.

According to the Bhaba Committee on the Examination of the Companies Act, 1913, particular provisions defining "Minority" should be included in the new Act to provide a reasonable framework. However, in order to represent the interests of the "Minority," the current Act provides 10% criterion for enterprises with share capital and 20% criteria for other companies.

⁴[(1934) 4 Comp Cas 434].

⁵ Mike Oluwaseyi Bamigboye, *The True Exception to the Rule in Foss v. Harbottle: Statutory Derivative Action Revisited*, Available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2863851 (Visited on 30 Jan 2020)

"Minority shareholders" are defined as shareholders with minority holdings in a corporation controlled by a majority shareholder; nevertheless, this definition is not included in the corporation Act of 1956. Usually the parent firm, the majority owners can also be an individual or a network of related shareholders.

The Suppressing shareholders are limited to 10% of shares under Section 395 of the Act. For the restricted purpose of exercising their rights before the relevant forum, a "minority" is defined as having no more than 10% of the shares.

Those who own a minimum number of shares in the corporation are often considered minority shareholders. Minority shareholders have some degree of power. Provisions granting a minority shareholder leverage to stop the majority from becoming overly large have always been present in the Companies Acts.

RIGHTS AND PRIVILEGES OF THE MINORITY SHAREHOLDERS UNDER THE COMPANIES ACT, 1956

On the advice of the Bhaba Committee, which was established in 1950 with the intention of fortifying the current corporate rules and establishing a fresh framework for corporate activity in independent India, the Companies Act 1956 was passed. The Companies Act 1913 was repealed in 1956 with the passage of this legislation.

The Companies Act of 1913 was modified with the primary goal of identifying ways to safeguard the interests of investors and stakeholders by providing a legal framework for good corporate governance, which includes small investors.

The rights of shareholders must be properly and efficiently affirmed in order to manage the business and to maintain a viable, sound environment. The following are some of the techniques that they have by virtue of statutes:

- A disgruntled shareholder may file an appeal with the tribunal challenging the company's denial of registering the share transfer.
- To ensure that the Central Government can protect the interests of the oppressed minority, a predetermined number of members may appeal to the Central Government for the

appointment of a certain number of people as directors of the firm.

- A company's contribution has the right to ask the court to wind it up in a fair and reasonable manner.
- Any member may rebuild a company's rebuilding or merger.
- During a company's winding up process, the liquidator or any creditor or contributor may request that the tribunal look into the actions of a delinquent official and take appropriate action.

PROTECTION OF THE RIGHTS OF MINORITY SHAREHOLDERS

Companies are increasingly using stock options as a recruiting tool for talented workers. Although these stock offerings can draw in and incentivize important staff members, they also give rise to a new class of shareholders known as minority shareholders, who have ownership interests but limited ability to actually affect corporate governance. To preserve minorities' rights, this regulation has developed with a few exceptions to the rule of majority shareholders, they are:

- **Act Ultra Vires:** The majority rule only applies when an act is permitted under the AOA or MOA; if an activity is outside the scope of the MOA or is illegal under the Companies Act, even a majority resolution will not be able to correct it. Therefore, the majority rule will be meaningless in these kinds of ultra vires act cases because any individual shareholder might file a suit to stop the firm from engaging in such illegal conduct.
- **Those in authority defrauding the minority:** The most significant case involving this idea is *Menier v. Hooper*⁶, where a defendant appointed a friend as a liquidator to shield himself from claims made by the company during the winding up process. In response to a lawsuit brought by a minority shareholder, the court found that Hooper had engaged in fraud by permitting even one member to bring legal action against him. **When someone's rights are violated:** By virtue of owning shares, shareholders are entitled to certain rights, including the ability to participate in general meetings, the right to receive dividends when they are paid, and other rights outlined in the AOA and MOA. Even a single shareholder

⁶Menier v. Hooper's Telegraph Words (1874) LR 9 CH APP 350.

may file a challenge if their right to vote, record their vote, or cast a ballot in a director election is violated; majority consent is not necessary in this case.

- **Oppression and mismanagement:** Corporate oppression and mismanagement are enduring problems that have long afflicted businesses and their workers. Reduced productivity, low morale, and lower profitability have been the outcomes of mismanagement in a variety of ways, including financial, ethical, and operational mismanagement. The Companies Act, 2013, Sections 241–246, is Chapter XVI, and provides protection against this kind of mismanagement and tyranny in India. Oppression and mismanagement were covered by two separate parts in the 1956 statute; however, the 2013 statute's section 241 now includes both.

The meaning of these terms should be inferred from the interpretation of judgments even though no statute defines them. But according to Lord Cooper, the essence of oppression is when "the conduct complained of seems to at the lowest involve a visible departure from the standards of fair dealing, and a violation of the conditions of fair play on which every shareholder who entrusts his money to the company is entitled to rely," as was the case in the landmark case *Elder v. Elder & Watson Ltd.*⁷

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Furthermore, as Mr. Cyrus Pallonji Mistry was complicit in the illegal conversion of the corporation from a "Public Company" to a "Private Company," the case of *Cyrus Investments (P) Ltd. v. Tata Sons Ltd.*⁸ concerned Mr. Mistry's reinstatement as Executive Chairman of Tata Sons Limited. The National Company Law Appellate Tribunal granted Mistry's request to be reinstated for the remainder of his tenure, initially as the Tata Group

⁷ 1952 SC 49 Scotland.

⁸ *Cyrus Investments Pvt. Ltd. & Ors.v Tata Sons Ltd. & Ors* MANU/NL/0640/2019 (India).

of Companies' "Executive Chairman" and then as a "Director."

- **The act requires a unique majority vote:** The majority rule as it developed from *Foss v. Harbottle* cannot be invoked as a defense by a simple majority in situations where a special majority is required, such as when certain acts require consent from a special majority, or 3/4 of the company's total members. Because of this, any individual employee of the firm has the ability to stop the company from moving forward with such a basic resolution if the crucial requirement of a special resolution is not taken into consideration.⁹

LANDMARK JUDGEMENTS

The Indian judiciary has made an effort to maintain a fair and impartial stance when protecting minority shareholders' interests relative to those of large shareholders.

The plaintiff in *Bharat Insurance Co. Ltd v. Kanhaiya Lal*¹⁰ was the respondent company's shareholder. The advance of funds at interest on the security of real estate, equipment, buildings, and other assets situated in India was one of the aim provisions. The plaintiff requested a permanent injunction to prevent the corporation from making further investments because it claimed that the company had made multiple investments without sufficient security and in violation of the memorandum's terms.

A single member may maintain a suit for declaration as to the true construction of the article in question in these circumstances. The court noted that the broad rule in such cases is undoubtedly that in all internal matters, a company's management is the best judge of its affairs and the court should not interfere. However, the application of the company's assets is not a matter of only internal management; it is alleged that the directors are acting ultra vires in their application of the company's funds.

The minority shareholder's attorney contended in a different case, *Sandvik Asia Ltd*¹¹, that while the majority has the authority to lower capital, it must do it in a fair and equitable manner. Minority stockholders in this instance were not given any options under the proposal. They were

⁹ *Bailey v. Oriented Telephone Company Ltd.* (1915) 1 CH 503 CA.

¹⁰ *Sh. Kanhaiya Lal vs Sh. Bharat Bhushan* on 16 May, 2015

¹¹ *Sandvik Asia Ltd vs Commissioner Of Income Tax-I, ...* on 27 January, 2006

given a deadline and instructed to either accept the offer and pay the suggested sum or leave the company. The court ruled that this was extremely unfair and unequal because minority shareholders were forced to leave the company and the majority could not just bully the minority out of existence.

The majority in *Needle Industries (India) v. Needle Industries Newey (India) Holding Ltd*¹². claimed oppression from a minority (Indian shareholder) because the minority was buying out the majority in accordance with government mandate that foreign shares (the majority) be sold to Indian shareholders. However, the court decided that the government's mandate, which required Indian minority shareholders to buy majority shares at market value, did not constitute an oppressive conduct.

CONCLUSION

Even now, majority rule—which was once a symbol of democracy—is still in place, but it is no longer mindlessly adhered to, and laws in many nations now follow it, albeit not as strictly as they did when the *Foss v. Harbottle* case became apparent. In the event that this account is not successful, the shareholders desire no further involvement in the business. It may not be worth much for them to keep their shareholding, with or without the ability to veto and participate in decisions. Nothing would be preferable in this situation than to incorporate a buy clause that would allow the parties to part ways.

A significant recommendation is that shareholders ought to be involved in both the nomination and the election of directors. Another proposal is to give shareholders an opportunity to be involved in the establishment of the Audit Committee, Compensation Committee, etc. Furthermore, proxy members ought to have the freedom to voice their opinions as well as the ability to vote.

¹² AIR 1981 SC 1298.