

INTERNATIONAL JOURNAL OF LAW
MANAGEMENT & HUMANITIES

[ISSN 2581-5369]

Volume 4 | Issue 6

2021

© 2021 *International Journal of Law Management & Humanities*

Follow this and additional works at: <https://www.ijlmh.com/>

Under the aegis of VidhiAagaz – Inking Your Brain (<https://www.vidhiaagaz.com/>)

This Article is brought to you for “free” and “open access” by the International Journal of Law Management & Humanities at VidhiAagaz. It has been accepted for inclusion in International Journal of Law Management & Humanities after due review.

In case of **any suggestion or complaint**, please contact Gyan@vidhiaagaz.com.

To submit your Manuscript for Publication at **International Journal of Law Management & Humanities**, kindly email your Manuscript at submission@ijlmh.com.

Minority Shareholder Rights: A Conundrum

PALOMITA SHARMA¹

ABSTRACT

It is a well-known fact that all decisions which are taken in a corporate democratic world are majorly based on the votes and choices of the majority. The rule laid down by the various provisions and landmark judgments, known as the Majority rule, tends to ignore and overpower the rights and decisions of the minority shareholders in a company. There is utmost power and significance given to the power of the majority in the working and functioning of a company and the rights of the Courts had been taken away by the Act of 2013 to intervene in the matters related to any shareholder rights or internal managerial issues. It is in such circumstances that the minority shareholders have to succumb to the decisions made by the majority of the people in the company on any related internal matter. Such matters in the management of a company can result into various issues, one of most significance being the emergence of an oppressive nature on part of the majority shareholders which may undermine the interests of the minority shareholders and in turn, also the best interests of the company if such oppressive decisions are taken in conditions notwithstanding the benefits of the company in the circumstance so put in. There are several provisions, as given under S. 397 to 409, which have been brought in by the Companies Act, 2013 as well as the concept of Piggy Backing that provide safeguards to the minority shareholders against oppression and any unjust decision making by the majority as well as a safe haven for the rights of the minority. This paper tends to throw light on the existence and importance of Minority rights under the Companies Act, 2013 as well as the various issues that the minority shareholders face while exercising their rights.

Keywords: *Minority, Shareholders, Majority Rule, Company, Companies Act, Internal Management, Non- Interference.*

I. INTRODUCTION

The Majority Rule, as stated under Article 47² provides that any member/shareholder holding equity shares in a company is entitled to vote on any decisions with respect to such an invested capital, if and when any decision making is brought in the company. The shareholders are given absolute rights to vote in consonance with the assets put into the company and those decisions

¹ Author is a student at Symbiosis Law School, Hyderabad, India.

² Section 47 of Companies Act, 2013.

may coincide with the preference of the shareholder. For any such decision to be binding and brought into force, a simple majority shall not be taken into consideration but rather a special majority where it is expected that a majority of 3/4th of the votes being put in the meeting by the members present should be in favour of the decision so being made and proposed. Such considerations are majorly specific and vital to matters which require a unique resolution³ under the articles of the Act. If such a decision is made with a special majority during the proceeding of a meeting, such a decision will be binding and legally enforceable on the minority shareholders.

In the case of *Foss v. Harbottle*⁴, the principle of the Non-Interference was implemented which states that the decisions of the majority shall be binding on the minority shareholders. According to this principle, the Courts are not allowed to interfere in any matters related to the internal managements of a company and can only intervene in cases where the powers are provided to such Courts by the Articles of Association of the company. The company is not empowered to cover or decided any situation or choice which is ultra vires its powers or is illegal in nature as against the minority shareholders.

II. MINORITY SHAREHOLDERS: WHO ARE THEY?

The corporate governance system must ensure that all owners are treated equally. When we talk of minority shareholders, the first thing that comes to mind is "what kind of minority will there be?" It is a legal term that is relative and whose meanings are largely dependent on the concept of plurality. The Bhaba Committee on the Companies Act of 1913 believed that by including explicit clauses to describe "minority"⁵ a fair definition might be established. The current Act, however, provides a ten percent criterion for companies which have a share capital and twenty percent likewise for companies which do not, in order to represent the interests of the "Minority." Dissenting owners are limited to 10% of the company's stock under Section 395⁶ of the Act. As a result, a "minority" may be described as anyone who owns less than 10% of a company's stock for the sole purpose of agitating their interests in the proper venue.

The word "minority owners" is not specified anywhere in the Companies Act of 1956. It can be understood as a person who owns less than half of the stock of a company and they do not have any management or voting powers⁷. Minority owners, in general, are those who own the

³ Bratton and Wachter, 'The case against shareholder empowerment', Vol. 2 (1987).

⁴ *Foss v. Harbottle* (1843) 2 Hare 461.

⁵ N. A Bastin, "Minority Protection in Company Law"(1968) JBL 320.

⁶ Companies Act, 1956, Section 395.

⁷ Paranjape, N.V Dr., "Company Law", (4th Edn. Rep.2011), Central Law Agency, Allahabad at p.440.

smallest amount of shares in a corporation. A minority shareholder may not have complete control over the business. The Companies Acts have long included clauses that give a minority shareholder power to restrain the majority's excesses.

III. MINORITY SHAREHOLDERS' RIGHTS UNDER THE COMPANIES ACT, 1956

The Companies Act of 1956 was passed in response to the recommendations of the Bhaba Committee, which was formed in 1950 with the aim of consolidating existing corporate laws and establishing a modern legal framework for corporate operations in independent India. The Companies Act of 1913 was amended with the passage of this statute⁸ in 1956. One of the main goals of the 1913 Companies Act amendment was to identify ways to safeguard the rights of creditors and customers, especially small investors, by establishing a regulatory framework for good corporate governance practices.

The following rights of the owners should be confirmed in order to establish a viable and sound atmosphere within a corporation and to manage the company successfully and efficiently.

The following are some of the rights granted to them by statute:

1. A shareholder who is dissatisfied with the company's failure to record a sale of stock may file a complaint with the Tribunal.
2. A provided percentage/number of these representatives can apply to the Government to seek selection of directors of the company as the Centre deems fit to protect the rights of these minorities.⁹
3. A corporation's contributory has the right to file a motion in court to get the company wound up on fair and equal grounds.
4. A company's reconstruction or amalgamation may be slowed down by any participant.
5. During the process of a company's winding up, the liquidator or other shareholder or contributory can request that the tribunal investigate and impose action against a delinquent officer.

IV. MINORITY INTERESTS REPRESENTATION

The Bhaba Committee believed that the idea of independent directors will be helpful in involving minority shareholder protection in managerial issues and discussions, decision making etc. It was noted that the current Act gave companies the option of using proportionate

⁸ Wedderburn, K.W.,"Unreformed Company Law",(1969) 32 Mad. LR 688.

⁹ Deval Patel, "Minority Shareholder Rights", CLSA U Speaker Series, January 2009.

representation for director appointments, but this method was seldom exercised. The applicability of Section 265¹⁰'s rules may be rendered obligatory¹¹, according to one viewpoint. Investor security may also be enhanced with the appointment of a minority-appointed director/independent director. The current alternative, in the Committee's opinion, should be held.

V. SHAREHOLDERS HAVE THE RIGHT TO BE UPDATED BY ACCURATE FILINGS

Via proper accountability and disclosures¹², investors' losses may be limited or decreased. All members shall have the right to receive information pertaining to the company within due time. Such information should not be difficult to comprehend for the members. This would improve the company's reputation and enable shareholders to make thoughtful and deliberate decisions about their investments. Apart from legislative records, which will be governed by statute, information may also be rendered accessible by various methods such as paper, electronic media, business websites, and so on. In the event that businesses access funding via stock offerings, a regime with strict transparency norms should be in place. Inappropriate leaks should be subject to adequate and deterrent legal sanctions.

VI. MINORITY SHAREHOLDER RIGHTS AT CORPORATE MEETINGS

It is widely seen that corporate meetings are usually inclined towards not hearing the concerns of the minority shareholders. The Bhaba Committee recommended guidelines should be helpful in curtailing this practice. These people have the power to attend general meetings, to request that a general meeting be called by the judge, to select proxies¹³ to attend and vote at general meetings, and to present proposals at shareholder meetings. To enable shareholders to engage in meetings, a large number of postal ballots, as well as electronic media, should be used.

VII. OPPRESSION AND MISMANAGEMENT OF RIGHTS

In order to deter oppression and mismanagement, the current Act has appropriate protections. Minorities can approach Courts/Tribunals for defense of their rights whether they are served by a certain number of representatives or if they own a certain amount of equity resources. The

¹⁰ Companies Act, 1956, Section 265.

¹¹ Dinah Spence, James Pheasant, "What rights minority shareholders have in Company Disputes – A situation that could affect both practitioners and their clients", ACCA, ISSN. 62, December 2003.

¹² "Minority Interests" ¶8.1 available at <http://www.mca.gov.in/Ministry/chapter6.html> Last Accessed on 7th April, 2021.

References

¹³ "Minority Interests" ¶8.4 available at <http://www.mca.gov.in/Ministry/chapter6.html> Last Accessed on 7th April, 2021.

quasi-judicial entity¹⁴ has the authority to impose a variety of corrective steps to regulate the operation of business relations. There can be steps like dissolution or setting the administration aside, reaching the Courts and Tribunals in extreme circumstances or curtailments of rights etc.

VIII. RIGHTS OF MINORITY SHAREHOLDERS DURING MERGERS/ AMALGAMATIONS/ TAKEOVERS

According to the Act's current rules, a company's corporate consolidation¹⁵ (which entails, among other things, mergers/amalgamations) requires the consent of the High Court or Tribunal. The owners should authorize the scheme before it is registered in any High Court. This scheme is then shared with all the members along with a notice of a Court called meeting and an explanatory statement under S. 393¹⁶ of the Act, which is mainly done to get the approval of the shareholders. Courts take a cautious approach in accepting the proposal by requiring that the proposed scheme be advertised in the newspaper to solicit any opposition from all the shareholders. Any involved party (including a minority shareholder) has the right to testify in front of the Court. However, there have been instances where owners of minor shareholdings have filed baseless challenges to the system with the sole purpose of delaying or delaying its adoption. Their objections have been overruled by the courts on many occasions.

To summarize:

- a) In cases of an amalgamation¹⁷, a minimum number or percentage of members should be established in order for them to object to the scheme and for it to be considered likewise,
- b) For making a reorganisation plan which is acceptable and appropriate, the provisions of S. 395A of the Companies (Amendment) Bill, 2003 can be used.

IX. A WAY OF SAFEGUARDING MINORITY RIGHTS, FAIR VALUATION

The assessment of a company's securities by an impartial valuation process should be recognized as a means to safeguard the rights of minorities. The Audit Committee is entrusted with choosing an impartial valuer for the process. If shareholders believe the procedure is unjust, they may be able to file a complaint with the court or tribunal. The Tribunal should have the authority to select an impartial valuer in such situations. These criteria for valuing

¹⁴ "Minority Interests" ¶9.1 available at <http://www.mca.gov.in/Ministry/chapter6.html> Last Accessed on 7th April, 2021.

¹⁵ Rule 7 of the Companies (Appointment and Qualifications of Directors) Rules, 2014.

¹⁶ Companies Act, 1956, Section 393.

¹⁷ Umakanth Varottil, Activism through Directors Elected by Small Shareholders, INDIA CORP LAW, (dated 25th July, 2017), available at <https://indiacorplaw.in/2017/07/activism-through-directors-elected-by.html> (last visited on 18th April., 2021)

securities may also be extended to firms that have delisted and have 1000 or more shareholders. In addition, the Committee suggested that any company that has a shareholder base of 1000 or more and has delisted itself from all the stock exchanges in India, should be mandated to make a buy back bid within 3 years of such delisting. The Committee believes that such a bid, when seen in light of the Committee's guidelines for maintaining equal share valuations, will also help to safeguard minority interests.

X. MINORITY RIGHTS: JUDICIAL PERSPECTIVES

In the case of *Foss v. Harbottle*¹⁸, the Inception of Majority Rule had beaked the rights of minority owners from the beginning. Although through various other judgements, there has been a curbing of the Majority Shareholder powers in order to form an equal platform of representation for all the members of the company. All of this came up through exceptions to the Majority Rule in various judicial decisions.

The following are some of the exceptions to judicial pronouncements:

The first exception is whether the suspected behaviour is deemed unconstitutional or ultravires the powers of the company. *Taylor v. National Union of Mineworkers*¹⁹ and *Smith v. Croft No. 2*²⁰ depict clearly that a member can also file a suit against a lawful act which is threatened in nature (as in *Simpson v. Westminster Palace Hotel Co.*²¹) and likewise also overturn an act which is unlawful in nature through the same course of action by the member.

A case where the issue so suspected may have been validly performed or has been accepted by a special majority as in the case of *Edwards v Halliwell*²². This case stated that the act in question should have been done only after a special majority and not a simple majority of votes by the members. Therefore, the rule given in *Foss v. Harbottle* cannot be relied on provided that the action was brought to protect individual rights and not the rights of the majority/union altogether. The accused had brought violated the minority's family's rights and individual interests by infringing the Union rights.

The third exception is the violation of individual rights of a member in his role as a participant. The fourth exception occurs in a case where a fraud has been committed with the minority by the majority shareholders.

The minority has been the victim of a variety of frauds. The case of *Menier v. Hooper's*

¹⁸ *Foss v. Harbottle* (1843) 2 Hare 461.

¹⁹ *Taylor v. National Union of Mineworkers*, [1985] IRLR 99.

²⁰ *Smith v. Croft No. 2*, [1988] Ch 114.

²¹ *Simpson v. Westminster Palace Hotel Co.*, [1860] Eng R 817.

²² *Edwards v Halliwell*, [1950] 2 All ER 1064.

Telegraph Works²³ is an example of corporate wealth misappropriation. The Court held that the rights of the minority were rightfully at risk when it was reported that there was a self-interested dealing between the company and a majority shareholder.

Templeman J. stated in the case of *Estmanco (Kilner House) Ltd v. Greater London Council*²⁴ that a minority is allowed to bring a claim even if no fraud has been reported. As a result, the Court determined that stultification of the company's original intent, despite the interests of minority shareholders, may be considered fraud on the minority.

XI. INDIAN JUDICIAL SYSTEM

The Indian judicial system has attempted to maintain a neutral perspective in order to protect minority shareholders' interests over those of dominant shareholders.

The plaintiff in *Bharat Insurance Co. Ltd v. Kanhaiya Lal*²⁵ was a shareholder in the respondent firm. The complainant claimed that "several investments have been made by the corporation without sufficient protection and counter to the terms of the memorandum and thus prayed for a permanent injunction to restrain it from making certain investments," according to one of the object clauses.

"The general rule in such cases is without a doubt that in all matters of internal control of a business, the company itself is the better judge of its affairs, and the court does not intervene," the court said. However, putting the company's money to use is more than just a question of internal control. The directors are accused of behaving against the law when it comes to using the company's money. Under certain cases, a sole member may file a declaratory judgment action to determine the nature of the scheme/article in question.

In *Sri Ramdas Motor Transport Ltd. v. Tadi Adhinarayana Reddy and Ors.*²⁶, the SC held that if any member claims that the working of the company is against the public order and interests or is violative of a members' rights is allowed to appeal to the NCLT under S. 397 of the Companies Act. The majority is likewise not stripped of their powers and rights.

Similarly, in *Shanti Prasad Jain v. Kalinga Tubes Ltd.*²⁷, which was a dispute between two major companies over the ownership of a particular corporation. It was accused that the company's relations were oppressive of him and a portion of the company's representatives. The claimant claimed that allotment of new stock to foreigners was for the purpose of

²³ *Menier v. Hooper's Telegraph Works*, (1874) 9 C App. 350.

²⁴ *Estmanco (Kilner House) Ltd v. Greater London Council*, [1982] 1 WLR 2.

²⁵ *Bharat Insurance Co. Ltd v. Kanhaiya Lal*, AIR 1935 Lah 729.

²⁶ *Sri Ramdas Motor Transport Ltd. v. Tadi Adhinarayana Reddy and Ors.*, AIR 1997 SC 2189.

²⁷ *Shanti Prasad Jain v. Kalinga Tubes Ltd.*, AIR 1965 SC 1535.

undermining established shareholders' interests and amounted to discrimination. The Supreme Court ruled that the High Court was correct in dismissing the case under Section 397²⁸ since the simple existence of allotment does not constitute injustice. The court stated that there would be compelling evidence to excuse mismanagement or injustice.

In the case of *Miheer H. Mafatlal v. Mafatlal Industries Ltd.*²⁹, the Supreme Court opined upon the restrictions on the control so imposed. The Court may only interfere in a matter if it is not right and equitable, or if it is detrimental to the interests of shareholders, according to the ruling. If the arrangement is approved by a plurality of shareholders and is legal, the court may not interfere. The only thing the court will do is look at the scheme to see how it meets the conditions of Section 391(2)³⁰ and was passed by the required majority. Individual personal interests of minority owners are of no consequence because the scheme approved by the corporation with a vote is right and equal and does not harm minority interests.

In another instance, *Sandvik Asia Ltd.*³¹, the minority shareholders' counsel claimed that although the majority has the power to minimize money, it must be done fairly and equally. Minority owners were not granted any options under the proposal in this situation. They were issued a deadline and informed that they had to consider the bid or quit the firm after getting compensated the sum accepted. According to the Court in this case, the minority's rights have been bulldozed as they were not left with any option but to leave the business. The majority should not have infringed the rights of the minorities.

Furthermore, in *Reckitt Benckiser (India) Ltd.*³², it was argued that the capital reduction plan was put through with malafide intentions and was discriminatory in nature such that it had an effort to remove the shareholders so that the investors could have complete ownership by purchasing 100 percent shares. "No question, the result of capital reduction is to extinguish public shareholding," the Delhi High Court said, "but if the objectors do not wish to part with their equities, the corporation shall not insist on it." The equity capital of any minority member is limited in a situation where not any of such members are opposed to the sale at the prices offered of their shares. As long as some are concerned, the objectors have no cause for complaint since their interests are protected."

²⁸ Companies Act, 1956, Section 397.

²⁹ *Miheer H. Mafatlal v. Mafatlal Industries Ltd.*, AIR 1997 SC 506.

³⁰ Companies Act, 1956, Section 391(2).

³¹ *Sandvik Asia Ltd. Case*, [2004] 50 SCL 413 (Bom).

³² *Reckitt Benckiser (India) Ltd.*, 122 (2005) DLT 612.

XII. CONCLUSION

The majority rule as discussed through the course of the present paper was enshrined in the landmark case of *Foss vs. Harbottle*. The rule as laid down in the present case, to simply put, states that the actions of a majority of a company and any decision such taken by them is automatically legally binding on all the related parties and stakeholders. Historically, this principle was viewed as a sign of liberalism. However, in India, this concept is diluted and not strictly followed. There is however a reprise as the Companies Act, 1956 provides multiple provisions protecting the minority shareholders against any exploitation at the hands of the majority. The move for protection and analysis of the minorities under the Companies Act in India were first enshrined as under the constitutional process³³. Minority shareholders will not be considered a significant part of the business under the 1956 Companies Act due to the organization being suppressed by a plurality. However, the 2013 Companies Act took several decisive steps to protect minority shareholders' interests in the corporation regardless of the existence of discrimination or mismanagement affecting minority shareholders' privileges. The primary aim of the legislation may also be to safeguard the interests of minority shareholders. It is of tantamount importance to understand that it is an essential and primary motive of the Act to protect such minority shareholders against any form of exploitation.

However, the problem exists not in the legislative text but in enforcement of such provisions under the legislation. As is true for any legislation, the protections enshrined under the legislation are termed successful when they are applied, and thereby such minority rights will be successful only once such rights of the shareholders are enshrined within the effective management of the company. Section 244, Companies Act 2013 provides a shortcoming in the way of a threshold under such Section that can be seen as a cause of concern. Even though the presence of such filters is unavoidable to vexatious/frivolous legislative action in the Courts and thereby wasting time, such restrictions under Section 244 make realistic application a difficult, almost impossible act to carry out.

Class action lawsuits do address the present issue. However, much more information about the same must be dispersed and awareness created for widespread use of such class action law suits. This reduces the number of prosecutions and empowers a community of people to bring facts against an offender on comparable grounds.

Additionally, the companies have taken steps to protect minority shareholders' rights. The term "piggybacking" is now being used. This allows for certain few key things. In a scenario where

³³ Bhandari, M.C., *Guide to Company Law Procedures*, 6th edition, Lexis Nexis.

the majority shareholders purchase the shares of such minorities, even the privilege granted to such minority shareholder is transferred as a part of the transaction. This also allows for transactions where the entire business can be sold and all of the outstanding shares may be bid.
