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[for the use of students] BY:

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Shareholder’s Democracy:
The idea of shareholders democracy in today’s corporate world denotes the shareholder’s supremacy in the governance of the business and affairs of corporate sector either directly or through their elected representatives. Democracy means the rule of the people, by the people and for the people. In that context the shareholders democracy means the rule of shareholders, by the shareholders and for the shareholders in the corporate enterprise, to which the shareholders belong. Precisely, it is a right to speak, congregate, communicate with co-shareholders and to learn about what is going on in the company. Under the companies Act, the power has been divided between two segments: One is the Board of Directors and the other is shareholders. Directors exercise their powers through meetings of board of directors and shareholders exercise their powers through general Meetings. Under section 291 of the Companies Act, a general power has been conferred on the Board of Directors.
So, the Companies Act has tried to demarcate the area of control of directors as well as that of shareholders.

Following are some of the businesses which are required to be transacted by shareholders:

(i). Alteration of Memorandum of Association and Article of Association;

(ii). Further issue of Share Capital;

(iii). To reduce the share capital of the company;

(iv). To approach Central Government for investigation into the affairs of the company;

(v). To appoint directors;

(vi). To increase or reduce the number of directors within the limits laid down in Articles of Association;

(vii). To cancel, redeem debentures etc.
Majority Powers and Minority Rights-

As a company is an artificial person with no physical existence, it functions through the instrumentality of the Board of directors who is guided by the wishes of the majority, subject, of course, to the welfare of the company as a whole. It is, therefore, a cardinal rule of company law that prima facie a majority of members of a company are entitled to exercise the powers of the company and generally to control its affairs. According to Section 87 of the Company Act, 1956, every member of a company, which is limited by shares, holding any equity shares shall have a right to vote in respect of such capital on every resolution placed before the company. Member’s right to vote is recognized as right of property and the shareholder may exercise it as he thinks fit according to his choice and interest. A majority of the members of the company enjoy the supreme authority to exercise the powers of the company and generally to control its affairs. But this is subject to two very important limitations. Firstly, the powers of the majority of members -
is subject to the provisions of the Companies Memorandum and Articles of Association. A company cannot legally authorize or ratify any act which being outside the ambit of the memorandum, is ultra vires of the company. Secondly, the resolution of a majority must not be inconsistent with the provisions of the Act or any other statute, or constitute a fraud on minority depriving it of its legitimate rights.

The Principle of Non-Interference[RULE IN FOSS vs. HARBOTTLE CASE]-
The general principle of company law is that every member holds equal rights with other members of the company in the same class. The scale of rights of members of the same class must be held evenly for smooth functioning of the company. In case of difference(s) amongst the members the issue is decided by a vote of the majority. Since the majority of the members are in an advantageous position to run the company according to their command, the minorities of shareholders are often oppressed. The company law provides for adequate protection for the minority shareholders when their rights are trampled by the majority. But the protection of the minority is not generally available when the majority ----------------
does anything in the exercise of the powers for internal administration of the company. The court will not usually intervene at the instance of shareholders in matters of internal administration, and will not interfere with the management of a company by its directors so long they are acting within the powers conferred on them under the Articles of Association of the company. In other words, the Articles are the protective shield for the majority of shareholders who compose the Board of Directors for carrying out their object at the cost of minority of shareholders. The basic principles of non-interference with the internal management of company by the court is laid down in a famous case of FOSS vs. HARBOTTLE, 67 ER 189;(1843) 2 Hare 461 that no action can be brought by a member against the directors in respect of a wrong alleged to be committed to a company. The company itself is the proper party of such an action.

The Case: In Foss vs. Harbottle, two shareholders, Foss and Turton brought an action on behalf of themselves and all other shareholders against the directors and solicitor of the company alleging that by their concerted and illegal transactions -
they had cased the company’s property to be lost to the company. It was also alleged that there was no qualified board. Foss and Turton claimed damages to be paid by the defendants to the company. It was held by the court that the action could not be brought by the minority shareholders although there was nothing to prevent the company itself, acting through the majority of its shareholders, bringing action. The wrong done to the company was not which could be ratified by the majority of members. The company(i.e. the majority) is the proper plaintiff for wrong done to the company, so the majority of members are competent to decide whether to commence proceedings against the directors.

Justification and Advantages of the Rule in Foss Vs. Harbottle case-
The justification in this case is that the will of the majority prevails. On becoming a member of a company, a shareholder agrees to submit to the will of the majority. The rule really preserves the right of the majority to decide how the company’
-affairs shall be conducted. If any wrong is done to the company, it is only the company itself, acting, as it must always act, through its majority, that can seek to redress and not an individual shareholder.

However, the main advantages that flow from the rule in Foss Vs. Harbottle Case are of a purely practical nature and are as below:

(i). Recognition of the separate legal personality of the Company;
(ii). Need to preserve right of majority to decide;
(iii). Multiplicity of futile suits avoided;
(iv). Litigation at suit of a minority futile if majority does not wish it.

EXCEPTIONS to the Rule:[Actions by shareholders in common law]
The rule in Foss vs. Harbottle is not absolute but is subject to certain exceptions. Some of these are below:
(i). Ultra Vires Act-
Where the directors representing the majority of shareholders perform an illegal or ultra vires act for the company, an individual shareholder has right to bring an action. The majority of shareholders have no right to confirm an illegal or ultra vires transaction of the company. In such case a shareholder has the right to restrain the company by an order or injunction of the court from carrying out an ultra vires act.

(ii). Fraud on Minority-
Where an act done by the majority amounts to a fraud on the minority; an action can be brought by an individual shareholder. This principle was laid down as an exception to the rule in Foss Vs. Harbottle in a number of cases.

(iii). Wrongdoers in Control-
If the wrongdoers are in control of the company, the minority shareholders representative action for fraud on the minority will be entertained by the court.
The reason for it is that if the minority shareholders are denied the right of action, their grievances in such case would never reach the court, for the wrong doers themselves, being in control, will never allow the company to sue.

(iv). Resolution requiring Special Majority but is passed by a simple majority-
A shareholder can sue if an act requires a special majority but is passed by a simple majority. Simple or rigid, formalities are to be observed if the majority wants to give validity to an act which purports to impede the interest of minority. An individual shareholder has the right of action to restrain the company from acting on a special resolution to which the insufficient notice is served.

(v). Personal actions-
Individual membership rights cannot be invaded by the majority of shareholders. He is entitled to all the rights and privileges appertaining to his status as a member. An individual shareholder can insist on the strict compliance with the legal rules, statutory provisions. Provisions in the Memorandum and the Article of Association are mandatory
in nature and cannot be waived by a bare majority of shareholders.

(vi) **Breach of duty**-

The minority shareholders may bring an action against the company, where although there is no fraud, there is a breach of duty by directors and majority shareholders to the detriment of the company.

(vii). **Prevention of Oppression and Mismanagement**-

The minority shareholders are empowered to bring action with a view to preventing the majority from oppression and mis-management.

**STATUTORY REMEDIES IN COMPANY ACT**-

Though the shareholder’s democracy is supreme, the company’s Act and the decided cases suggest that the majority shall not be allowed to act in an unfair, fraudulent, or oppressive way against the interest of the minority shareholders. Under section 38, 167, 388-B, 397, 398 and 399 various powers are given to the
shareholders. Further, under section 265, a company may adopt principal of proportional representation. Under section 408, the central government may direct the company to amend its Articles providing for appointment of directors according to principal of proportional representation under section 265 and make fresh appointment in pursuance of the Articles so amended within such time as may be specified. The company’s Act, 1956, extends protection to minority by granting various rights to minority shareholders.

**PREVENTION OF OPPRESSION AND MISMANAGEMENT:**

**Prevention of Oppression(Section 397)-**

The first remedy in the hands of an oppressed minority is to move the Company Law Board. Section 397 provides that any member of a company who complain that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member(s) may make an application to the Company Law Board by way of petition for relief.
Following requirements must be satisfied for seeking a relief under Section 397:

(i). That the affairs of the company are being conducted: (a) in a manner prejudicial to public interest; or (b) oppressive to any members.

(ii). That the fact justified the compulsory winding up order on the ground that it is just and equitable that the company should be wound up.

(iii). That to wind up the company would unfairly prejudice the petitioners.

The words “oppression” and “mismanagement” are not defined in the Act. The meaning of these words for the purpose of company law should be used in a broad generic sense and not in any strict literal sense.
WINDING UP ORDER UNDER JUST AND EQUITABLE CLAUSE:
The other requirement is that the facts justify the making of a winding up order under just and equitable clause. The principle is that if there is persistent violation of the regulations and statutes and an appeal to general body is not likely to put an end to the matters complained of by reason of the fact that those responsible for the violations control the affairs of the company, then it will be just and equitable to wind up the company.

PREVENTION OF MISMANAGEMENT[Section 398]:
Section 398 provides for relief in cases of mismanagement. For a petition under this section to succeed, it must be establish that the affairs of the company are being conducted in a manner prejudicial to the interest of the company or public interest, or that, by reason of any change in the management and control of the company, it is likely that the affairs of the company will be conducted in that manner. If the court is so convinced, it may, with a view to bringing to an end or preventing the matter complained of or apprehended, make such order as it thinks fit.
Persons Entitled to Apply:

The number of members required to make application under section 397 and 398 (i.e. who must sign the application) is given in section 399. It provides that where the company has a share capital, the application must be signed by at least 100 members of the company or by 1/10\textsuperscript{th} of the total number of the members, whichever is less; or by any member or members holding not less than 1/10\textsuperscript{th} of the issued share capital of the company. If the company has no share capital, the application has to be signed by at least 1/5\textsuperscript{th} of the total number of its members. The Central Government may, however, allow any member/members to apply, if in its opinion, circumstances exist which make it just and equitable to do so. The contents of such an application should fulfill the requirements laid down in Rule 13 of the Companies (central Government’s) general Rules and Forms, 1956.
POWERS OF THE COMPANY LAW BOARD (section 402) and POWERS OF THE CENTRAL GOVERNMENT TO PREVENT OPPRESSION AND MISMANAGEMENT:

Powers of the CLB under section 397 and 398 are fairly wide. In fact the court may make any order for the regulation of the conduct of the company’s affairs upon such terms and conditions as may, in the opinion of the court, be just and equitable in all the circumstances of the case. Apparently the only limitation seems to be the overall objective of the sections and therefore, the order must be directed to bring to an end to the matter complained of. However, an attempt is made under section 402 to define the powers of the CLB.

The Act not only confers special powers upon the CLB to prevent oppression or mismanagement, but also confers extra ordinary powers upon the central government to attain the same end.
The Central Government may appoint such number of persons specified in writing to hold office as directors thereof as is necessary to effectively safeguard the interest of the company, its shareholders or the public interest, for such period, not exceeding 3 years on anyone occasion as it may think fit, if the company Law Board considers it necessary to make the appointment in order to prevent the affairs of the company being conducted either in a manner which is oppressive to any members of the company or in a manner which is prejudicial to the interest of the company or to public interest.

[SPECIAL NOTE: Read the provisions of Oppression, Mismanagement and Dissolution of Company as per old Companies Act, 1956. [You may refer new Company Act, 2013 side by side. But, you should know both in order to understand clearly]