

20Th Century Finance Corporation Ltd. vs Rfb Latex Ltd. And Ors. on 29 June, 1999

Equivalent citations: [1999]97COMPCAS636(CLB)

ORDER

S. Balasubramanian, Chairman

1. In this petition filed under Section 397/398 of the Companies Act, 1956 ("the Act"), in the matter of R.F.B. Latex Limited (the company), the respondents have filed an application, C. A. No. 213 of 1998, in terms of Section 8 of the Arbitration and Conciliation Act, 1996 (the Arbitration Act), seeking for referring the parties to arbitration on the grounds stated in the application.

2. The allegations of the petitioner in this petition relate to the following :

- (a) Failure to amend articles of association to conform to the sponsorship agreement.
- (b) Delayed payment of dividend.
- (c) Default in lease payment to the petitioner.
- (d) Irregularities in rights issue.
- (e) Irregularities in respect of board meetings.
- (f) Fabrication of the minutes of board meetings.
- (g) Second expansion project/fabrication of company records.
- (h) Obtaining loan from IDBI in violation of the sponsorship agreement.
- (i) Siphoning off of funds and non-disclosure of interest.
- (j) Failure to co-operate with the auditors.

With these allegations, the petitioners have sought for various reliefs, inter alia, including directions to the company to amend the articles of association in line with the terms of the sponsorship agreement, ordering payment of interest at 24 per cent. on the delayed payment of dividend, for declaration that the board meeting dated December 7, 1996, and March 31, 1997, as null and void due to non-issue of notices for the meeting to the petitioners, direction to the company to terminate all arrangement and agreement relating to the second expansion project, restraining the company from utilising the funds raised by way of rights issue, ordering a special audit of the company, for a

declaration that respondents Nos. 2 to 4 have conducted the affairs of the company in total violation of the provisions of the Act, etc.

3. Shri Anil Sharma, advocate for the applicant/respondents, submitted that the petitioner-company had entered into a sponsorship agreement with the company dated October 6, 1994, by which the petitioner was to sponsor the company for listing and act as market maker for the shares and the petitioner was to subscribe to 10 lakhs equity shares of Rs. 10 each at a premium of Rs. 15, aggregating to Rs. 2.5 crores and that these shares were to be offered to the public before September, 1996. Therefore, by this agreement, there was an obligation on the part of the petitioner to list the shares in OTCEI which they had failed to discharge. The sponsorship agreement stipulates that any claim dispute or differences between the parties arising out of or in relation to or under or in any manner connected with the agreement shall be referred to and decided by arbitration as provided in the rules and regulations of OTCEI. Since the foundation of the petition is based on the sponsorship agreement and since most of the allegations relate to the said agreement, he submitted that in terms of Section 8 of the Arbitration Act, the Company Law Board is required to refer the parties to arbitration. Referring to the allegations relating to failure to amend the articles to conform to the sponsorship agreement, rights issue, second expansion, loan from IDBI, non-co-operation with the auditor, etc., he submitted that these allegations directly arose out of the terms of the agreement and as such the petitioner has to invoke the arbitration clause in the agreement and cannot agitate the same before the Company Law Board through this petition. Even other allegations are either directly or indirectly connected with the terms of the sponsorship agreement. Therefore, learned counsel submitted that the petition should not be entertained and the parties should be referred to arbitration. Otherwise, he urged, the petitioner should amend the petition deleting all references to the sponsorship agreement and agitate only those which are not arising out of the said agreement. In this connection, he referred to the Company Law Board decision in *Naveen Kedia v. Chennai Power Generation Ltd.* [1999] 95 Comp Cas 640 and *Escorts Finance Ltd. v. G.R. Solvents and Allied Industries Ltd.* [1999] 96 Comp Cas 323 (CLB) wherein the Company Law Board declined to entertain the petitions and referred the parties to arbitration in terms of Section 8 of the Arbitration Act.

4. Shri Dholakia, senior advocate appearing for the petitioner, submitted that the petitioner has invested about Rs. 2.5 crores in the share capital of the company and is a substantial shareholder. The allegations in the petition relate to various acts of oppression and mismanagement in the affairs of the company, against which as a substantial shareholder, the petitioner is entitled to file this petition. He pointed out that the sponsorship agreement consists of two parts--one, about the petitioner becoming a shareholder and the second, regarding the undertaking of certain obligations. Having become a member, the petitioner has got all the rights of a shareholder as envisaged in the Act. He submitted that in terms of Section 9 of the Act, the provisions of the Act override the memorandum and articles and any other agreement which are repugnant to the provisions of the Act. Since Sections 397 and 398 give a statutory right to the shareholders to move the Company Law Board in case of oppression and mismanagement, the statutory right conferred by the statute cannot be defeated by a private arbitration agreement. For this proposition, he relied on *Surendra Kumar Dhawan v. R. Vir* [1977] 47 Comp Cas 276 (Delhi) in which the Delhi High Court held that the statutory right to apply under Section 397/398 cannot be ousted by a provision in the articles, in

view of the provisions of Section 9 of the Act. Further, he pointed out that in the earlier hearings, the respondents never raised the issue of arbitration when the question of amicably settling the disputes was discussed before the Company Law Board and as such it should be presumed that the respondents have already submitted to the jurisdiction of the Company Law Board. The provisions of Section 8 are to be invoked before submitting the first statement on the substance of the petition but the respondents have already, by discussing the settlement proposals, dealt with the merits of the case. Section 8 does not stipulate that the submission on the substance should be in writing and, therefore, even oral submission on the substance would disentitle the respondents from invoking the provisions of Section 8. He submitted that the sponsorship agreement has been referred to in the petition only for the purposes of indicating the relationship between the parties and not for the purposes of enforcing the terms of the agreement. The allegations in the petition, learned counsel pointed out, cover various issues like failure to issue notices for the board meetings, siphoning off of funds, non-payment of dividend, etc., which do not arise out of the arbitration agreement. According to him, the petition is essentially against the affairs of the company and the persons who are in management with the allegation that the affairs of the company are being carried on in a manner prejudicial to the interest of the shareholders and public interest. He further submitted that in an arbitration only the financial claims between the parties can be settled and in the present case, no financial claims have been made by the petitioner against the respondents. He further submitted that the sponsorship agreement was to be in force only for a period of three years, i.e., up to October, 1997, and, therefore, relying on the sponsorship agreement in respect of the arbitration clause now in 1998, does not arise as when the provisions of Section 8 of the Arbitration Act are invoked, then, the arbitration agreement should be subsisting, which is not the position in the present case. Therefore, according to him, while in terms of Section 9 of the Companies Act, the Company Law Board is bound to entertain the petition, even otherwise, since many of the allegations relate to matters independent of the terms of the sponsorship agreement, the question of referring the parties to arbitration does not arise and, therefore, the application should be dismissed.

5. We have considered the pleadings and arguments of counsel, Shri Dholakia, referred to Section 9 of the Act to state that no provision of any agreement can take away the statutory rights conferred by the Companies Act and he also relied on a Delhi High Court case in this regard. Section 9 of the Act deals only with memorandum, articles or any agreement or any resolution which are repugnant to the provisions of the Act and does not deal with the provisions of other statutes. As a matter of fact, Section 5 of the Arbitration Act which reads "notwithstanding anything contained in any other law for the time being in force, in matters governed by this part, no judicial authority shall intervene except where so provided in this Act" makes it clear that in case of an arbitration agreement, a judicial authority cannot intervene except as provided in the Arbitration Act, notwithstanding anything contained in any other law. Section 8(1) of the Arbitration Act, 1996, reads as follows "a judicial authority before which an action is brought in a matter which is the subject of an arbitration agreement shall, if the party so applies not later than when submitting his first statement on the substance of the dispute refer the parties to arbitration". The Company Law Board being a judicial body is bound, in terms of Section 8 of the Arbitration Act, to refer the parties to arbitration if the allegations arise out of the terms of an agreement containing an arbitration agreement as defined in Section 7 of that Act, notwithstanding the provisions of Section 9 of the Companies Act. In other

words, Section 9 of the Act does not affect a right of a shareholder to invoke the provisions of Section 8 of the Arbitration Act in case there is an agreement to refer the disputes to arbitration. In the case of *Surendra Kumar Dhawan v. R. Vir* [1977] 47 Comp Cas 276 (Delhi), the Delhi High Court was dealing with a provision in the articles relating to arbitration, which the High Court held that the same cannot act as a bar for entertaining a Section 397/398 petition. Therefore, this case is not applicable in terms of the provisions of the Arbitration Act. In the two cases cited by learned counsel for the applicants/respondents, we declined to entertain those petitions filed under Section 397/398 of the Act and referred the parties to arbitration since the allegations contained in those petitions directly related to the terms of agreements which contained an arbitration clause.

6. Learned counsel for the petitioner submitted that the respondents having already submitted to the jurisdiction of the Company Law Board while discussing the terms of settlement, cannot now invoke Section 8 of the Arbitration Act, since the provisions of the section are to be invoked before submitting the first statement on the substance of the disputes. According to him, even making an oral statement on the substance of the disputes, would disentitle the petitioner from making this application. Even though, Section 8 of the Arbitration Act does not clearly state that the first statement should be in writing, yet, we have to presume that the same should be in writing, as an oral statement cannot normally be taken as a formal pleading in the absence of an affidavit in writing. Even otherwise, discussions on amicable settlement cannot be considered as a statement on the substance of the dispute. Therefore, we do not consider that by participating in the discussion for amicable settlement, the respondents have forfeited their right to invoke the provisions of Section 8 of the Arbitration Act. Yet another point raised by learned counsel was with reference to the currency of the agreement. According to him, the currency of the agreement expired in October, 1997, in terms of Clause 1.2 of the agreement and as such the agreement is not subsisting on the day when the present application was filed and, therefore, the Company Law Board referring the parties to arbitration does not arise. While it seems that there is substance in this argument, yet we find that in Clause 8.7 it is stipulated that the terms of the agreement shall be binding on the company as long as the petitioner holds shares in the company. The contradiction in these two clauses is something which the arbitrator has to decide. As far as the Company Law Board is concerned, as long as there is an arbitration agreement, then in terms of Section 8 of the Arbitration Act, the Company Law Board is bound to refer the parties to arbitration. Thus we find that there is no merit in the contention of the counsel for the petitioner that the application is not maintainable.

7. Now, the issue for examination is as to what is covered in the arbitration agreement to decide whether the matter before us is covered in the arbitration agreement. Article 8.2 of the sponsorship agreement reads "any claim, disputes or differences between the parties hereto arising out of or in relation to or under or in any manner connected with the agreement shall be referred to and decided by arbitration as provided in the rules, bye-laws and regulations of OTCEL.... Such arbitration shall be governed by the provisions of the Arbitration Act, 1940, or any modification or re-enactment thereof. The arbitration shall be held in Bombay only". It is clear that this clause not only deals with claims but also disputes and differences between the parties to the agreement. As long as the disputes or differences relate to the terms of the sponsorship agreement, then, the parties are bound to take recourse to arbitration. We have now only to consider whether the allegations contained in the petition arise out of or in relation to or under or are in any manner connected with the

sponsorship agreement, to decide whether the parties should be referred to arbitration in terms of Section 8 of the Arbitration Act.

8. We have already indicated the allegations contained in the petition, in a nut shell, in para. 2. From those allegations it can be seen that the allegations relating to failure to amend the articles, rights issue, second expansion project, loan from IDBI, failure to co-operate with the auditors, are grievances arising directly out of the sponsorship agreement and as such they cannot be agitated in the present proceedings in view of the arbitration clause. Yet there are other allegations which are independent of the sponsorship agreement, which an arbitrator cannot adjudicate for want of jurisdiction. According to the petitioner, these allegations exhibit acts of oppression and mismanagement in the affairs of the company. If it is so, then the Company Law Board is bound to examine the same. Whether the allegations merit grant of any relief or not is a matter to be decided after the pleadings are completed and arguments concluded. The facts of Escorts Finance Ltd. v. G.R. Solvents and Allied Industries Ltd. [1999] 96 Comp Cas 323 (CLB) are different from the present one, inasmuch as, all the allegations in that case wholly related to a sponsorship agreement in which there was an arbitration clause and, therefore, the Company Law Board declined to entertain the petition and referred the parties to arbitration. In a recent case of Khandwala Securities Ltd. v. Kowa Spinning Ltd. [1999] 97 Comp Cas 632 (CLB) in which also there were allegations in respect of matters covered in a sponsorship agreement covered by an arbitration clause as also matters independent of the agreement, we dismissed the application filed under Section 8 of the Arbitration Act, and directed the respondents to file a reply on the allegations which were independent of the sponsorship agreement.

9. In view of our finding that there are allegations in the petition independent of the sponsorship agreement, the prayer of the respondents in C. A. No. 213 of 1998, to refer the parties to arbitration and dismiss the petition is rejected. The respondents should file their replies covering all the allegations in the petition other than those at sub-paras (a), (d), (g), (h) and (j) of para. 2 above by August 1, 1999, and rejoinder, if any, will be filed by September 1, 1999. The petition will be heard on November 1, 1999, at 10.30 a.m.