**QUASI-PARTNERSHIP**

It is a form of a ‘closely held corporation’. It is run on partnership principles and all members have the **legitimate expectation** to be included in the management in accordance with the ‘equitable considerations’ that are present in a partnership firm.

The principle for this was laid down to grant remedy against an unfair prejudice claim where the minority shareholders were excluded from the management in the landmark English case of *Ebrahimi* v. *Westbourne Galleries* [1973] AC 360, where it was held that the following **criteria** need to be satisfied:

**Criteria:** “*(i) an association formed or continued on the basis of a personal relationship, involving mutual confidence - this element will often be found where* ***a pre-existing******partnership*** *has been converted into a limited company; (ii)* ***an agreement, or understanding, that all, or some (for there may be 'sleeping' members), of the shareholders shall participate in the conduct of the business****; (iii)* ***restriction upon the transfer of the members' interest*** *in the company - so that if confidence is lost, or one member is removed from management, he cannot take out his stake and go elsewhere.*”

**Cases**

* Sangramsingh P. Gaekwad v. Shantadevi P. Gaekwad, AIR 2005 SC 809.

*“****It is now well-known that principles of******quasi-partnership is not foreign to the concept of Companies Act***”

“*It is, however, one thing to say that for the purpose of dealing with an application under Section*[*397*](javascript:fnOpenGlobalPopUp('/ba/disp.asp','19026','1');)*of the Companies Act, the court would not easily accept the plea of quasi-partnership but as has been held in Needle Industries (supra), the true character of the company and other relevant factors shall be considered for the purpose of grant of relief having regard to the concept of quasi-partnership*.”

* M.S.D.C Ramadharan v. M.S.D Chandrasekara Raja and Anr., AIR 2008 SC 1738

Deadlock described at Para 13 - “*The deadlock in regard to the conduct of the business of the company has been noticed by the Company Law Board as also the High Court. Keeping in view the fact that there are only two shareholders and two Directors and bitterness having crept in their personal relationship, the same, in our opinion, will have a direct impact in the matter of conduct of the affairs of the company. When there are two Directors, non-cooperation by one of them would result in a stalemate and in that view of the matter the Company Law Board and the High Court have rightly exercised their jurisdiction*”; and at Para 27 CLB and HC’s findings of deadlock were confirmed.

Quasi-partnership was applied due to the nature of the company being a closely held corporation – two shareholders only in a family run business with mutual understanding with regard to rights in management “*In a case of this nature, it is necessary to take a holistic approach of the matter*. ***What might not be permissible for the affairs of a public limited company or even a private company having large number of shareholders and Directors, may be permissible in a case of this nature where a company for all intent and purport a quasi-partnership concern****.*”

In this case, it was opined that the ‘just and equitable’ clause (under s. 397 of Companies Act, 1956, corresponding to s. 292) is “*essentially an equitable consideration, and may be superimposed on law*”, similar to the English law position in Ebrahimi v. Westbourne Galleries.

* In re Yenidje Tobacco Co. Ltd. (1916) 2 Ch 426

This was a company of two shareholders and two directors who had earlier traded separately but amalgamated their businesses and formed a private limited company. The Constitution of the company was such that under its articles of association for any case of difference or dispute between the directors there was a provision for arbitration. In one of such disputes a reference was made to arbitration which resulted in an award to which one of the two shareholders declined to give effect. It was proved in that case that the two directors were not on speaking terms, that the meetings of the board of directors had been almost a farce, the directors would not speak to each other on the board, and some third person had to convey communications between them which ought to go directly from one to the other.

“**If ever there was a case of deadlock I think it exists here; but, whether it exists or not, I think the circumstances are such that we ought to apply, if necessary, the analogy of the partnership law**”

This case was followed by The Supreme Court in **Hind Overseas (Private) Ltd. v. Raghunath-prasad Jhunjhunwala** [1976] 46 Comp Cas 91, where, while deciding the appeal on the judgment of the Division Bench of the Calcutta High Court it held that it is only when the **shareholding is more or less equal** and there is a case of complete **deadlock** in the company on account of **lack of probity** in the management of the company and there is no hope or possibility **of smooth and efficient continuation** of the company as a commercial concern, that there may arise a case for winding up on "just and equitable" grounds. (paragraph 32)

* Yashovardhan Saboo v. Groz Beckert Saboo Ltd*.,* (1995) 83 Com Cases 371 (CLB).

A closely-held company was composed of two groups one foreign and one local, holding as between themselves respectively 60%: 40% shares. The articles of the company contained all the matters of their mutual understanding which included provisions enabling them to enjoy equal amount of managerial power. The differences arose between them which prevented them from collaborating with each other and leading to a state of deadlock. The CLB applied the *quasi*-partnership principles and ordered the majority group to buy out the minority at the fair price with necessary permissions. (Paragraph 62)

* Phoenix Office Supplies Ltd & Ors v Larvin, [2002] EWHC 591 (Ch)

It followed that the company was a quasi-partnership company in which the exercise of legal rights was subject to equitable constraints designed to **ensure the maintenance of their common understanding concerning their right of participation in the management of the company and the enjoyment of their shareholder rights**. (Para 41)

Other Cases :- In determining rights of “partners” for winding up under ‘just and equitable’ ground regard must be had to not merely what the articles say, but also to what the parties are shown to have agreed in any other manner. (Re Fildes Brothers Ltd. [1970] 1 All E.R. 923 at 926);

Just because the company is a listed company, it does not mean that principles of quasi-partnership cannot be applied. *“after discussing various decided cases, practically all the objections as in this case were examined by this Board and it concluded that to treat a company as a partnership, it was not necessary to have equal shareholdings, no need for deadlock, no need for pre-existing partnership etc. It also observed that an analysis of various decisions showed that courts have been looking for some basic understanding written or unwritten between parties. Therefore, if the facts reveal some basic understanding between parties that the company would be managed on partnership principles, then the same could be applied*” (Gurmit Singh v. Polymer Papers, 2005 123 CompCas 486 CLB)

**EFFECTS OF QUASI-PARTNERSHIP**

1. **Interpretation of term ‘shareholders’ to include directors as well**

* Karedla Suryanarayana v. Shri Ramdas Motor Transport Pvt. Ltd., [1999]98CompCas518(CLB)

The Company Law Board re-emphasised the already established principles that complaints in the capacity of directors can constitute the subject-matter of a proceeding only when the company is a closely held company and directors are in essence like the partners of a firm. The decision was **approved** by the A.P. High Court in *Sri Ramdas Motor Transport Ltd. v. Karedla Suryanarayana,* (2002) 110 Com Cases 193: (2002) 36 SCL 361 (AP)

“*Directorial complaints cannot generally be agitated, except in cases of closely held companies, wherein the right to hold directorial position has been provided in the articles or the principles of quasi-partnership with right to participate in management is established.”*

* Alexander Edward Jackson v. Patrick Giles Gauntlet and Reade, [2012]EWHC 2060(Ch)

In this case, a clause in the articles of the company provided for removal of directors upon, inter alia, giving of notice by other directors

“*Sub-paragraph (e) gives rise to altogether different considerations. It is a form of provision commonly to be found in partnership articles, and may be supposed to have been transposed to TFG because it was (at least as between its founders) a**quasi partnership company****. It is specifically designed to enable the directors (or partners) to remove a colleague without showing cause, enabling the parties to bring about a form of business or corporate "no fault" divorce where partners (including quasi corporate partners) have fallen out****, it is clear that the minority must go, but neither clear, nor necessarily provable, that the minority is the party at fault*.”

As stated above, **the court reasoned that the partners (who were the owners) may also find cause to remove the directors**, apart from the directors themselves exercising their rights.

* SHAREHOLDER AGREEMENTS IN CLOSELY HELD CORPORATIONS: IS STERILIZATION AN ISSUE? by Steven N. Bulloch

“*The dichotomy between owners (shareholders) and managers (directors and officers) present in a publicly held corporation does not exist in a closely held corporation because the shareholders of a closely held corporation are also involved in the management of the corporation; their roles as managers and owners are inseparable. The degree to which a shareholder agreement in a closely held corporation impinges on the statutory norm of director control, be it extreme or slight, is irrelevant because the norm serves no purpose in a closely held corporation. The same people who own the corporation are also its directors, and there is no group of passive investors relying on the board of directors to use its independent judgment on the group's behalf.*”

* Closely Held Corporations: An Intersection of Business, Law, and Ethics; By Orrin K. (Skip) Ames Iii 43 Cumb. L. Rev. 171 (2013)

“*In contrast to the more traditional corporate structure, closely held corporations have distinct differences that distinguish them from the more traditional corporate forms: (1) there is usually a small number of shareholders; (2)* ***in contrast with the clear lines of demarcation between the shareholders, governing board, and management in larger corporations, the functions of closely held corporations are compressed into a governance structure where the shareholders, management, officers, and board members are comingled****;" (3) whereas traditional corporations' shares of stock are freely sold and, absent external market conditions, are liquid, closely held corporations' shares are not easily sold or marketed; liquidity, therefore, is much reduced, or even absent," resulting in a more captive, dependent, and vulnerable ownership****. As contrasted with traditional corporate forms, where the spheres of influence are defined and separate, yet tethered by contractual relationships and fiduciary duties, the spheres of influence in close corporations are conflated, thus blurring the lines between them***.”

“*As demonstrated earlier, in the discussion of closely held corporations, the spheres of influence, boards, officers, managers, employees, and shareholders, are conflated.* ***The board members are the shareholders; the officers are the shareholders; the managers are the shareholders; the employees are the shareholders; the shareholders occupy all of these traditional spheres of influence****. Depending on the structure chosen, they are a cohesive organization working toward building the venture into a successful organization. That is, of course, until a breakdown occurs and the organization becomes dysfunctional as a result of self-dealing, unfulfilled expectations, and other areas of conflict*.”

* American case: Donahue v. Rodd Electrotype Co., 328 N.E.2d 505, 515 (Mass. 1975).

It was held that shareholders in a closely held corporation are more comparable to partners in a partnership than to shareholders in a public corporation, so that their relations should be governed by partnership-style obligations.

1. **Legitimate expectation arising out of the SHA and**

**2A) Oppressive Conduct arising out of breach of legitimate expectation**

* *In re Westbourne Galleries Ltd.* [1973] A.C. 360;

“*The words ['just and equitable'] are a recognition of the fact that a limited company is more than a mere legal entity, with a personality in law of its own: that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se which are not necessarily submerged in the company structure. That structure is defined by the Companies Act [1948] and by the articles of association by which shareholders agree to be bound. In most companies and in most contexts, this definition is sufficient and exhaustive, equally so whether the company is large or small. The 'just and equitable' provision does not, as the respondents [the company] suggest, entitle one party to disregard the obligation he assumes by entering a company, nor the court to dispense him from it.* ***It does, as equity always does, enable the court to subject the exercise of legal rights to equitable considerations; considerations, that is, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way***.”

* *O’ Neill* v. *Philipps*, [1999] 1 WLR 1092

It was held that where shareholders have entered into the company with the expectation that they will get to participate in the management, due to some agreement between them, and they are denied the opportunity by use of voting power by majority, it will be oppressive conduct.

“*But I think that one useful cross-check in a case like this is to ask whether the exercise of the power in question would be contrary to what the parties, by words or conduct, have actually agreed. Would it conflict with the promises which they appear to have exchanged? In Blisset v. Daniel the limits were found in the "general meaning" of the partnership articles themselves.* ***In a quasi-partnership company, they will usually be found in the understandings between the members at the time they entered into association.*** *But there may be later promises, by words or conduct, which it would be unfair to allow a member to ignore. Nor is it necessary that such promises should be independently enforceable as a matter of contract. A promise may be binding as a matter of justice and equity although for one reason or another (for example, because in favour of a third party) it would not be enforceable in law*.”

Lord Hoffman cited a previous decision and stated that the legitimate expectation is a consequence of the equitable considerations, not a cause.

“In *In* *re Saul D**Harrison & Sons Plc*. [1995] 1 B.C.L.C. 14, 19, I used the term "legitimate expectation," borrowed from public law, as a label for the "correlative right" to which a relationship between company members may give rise in a case when, on equitable principles, it would be regarded as unfair for a majority to exercise a power conferred upon them by the articles to the prejudice of another member. I gave as an example the standard case in which shareholders have entered into association upon the understanding that each of them who has ventured his capital will also participate in the management of the company**. In such a case it will usually be considered unjust, inequitable or unfair for a majority to use their voting power to exclude a member from participation in the management without giving him the opportunity to remove his capital upon reasonable terms. The aggrieved member could be said to have had a "legitimate expectation" that he would be able to participate in the management or withdraw from the company**.”

* Gurmit Singh v. Polymer Papers, 2005 123 CompCas 486 CLB

“*25. Further, the petitioners have also invoked the principles of legitimate expectations.* ***In cases of legitimate expectations, the denial of the same could be considered to be an act of oppression. For the authority on the principles of legitimate expectations reference could be made to Boyle & Birds' Company Law III Edition wherein it is stated that In a quasi-partnership type company, the Court may take account of legitimate expectations of members.****" In Re Elgindata Ltd.: [1991] BCLC 959 it has been held that "In general members of a company have no legitimate expectations going beyond the legal rights conferred on them by the constitution of the Company, i.e., to say its Memorandum and Articles of Association. Nonetheless legitimate expectations super imposed on a member's legal rights may arise from agreements or understanding between the members. In Atmaram Modi v. ECL Agrotech (1999 98 CC 463) this Board has held that in the course of business of a partnership, a partner is entitled to have certain legitimate expectations. Now in the present case, even assuming that no reliance can be made on the first MOU and that the Articles do not provide for continued appointment of Shri Gurmit Singh as an MD, whether the principles of legitimate expectations could be applied.* ***In Shri Dipak Mehta v. Shree Anupar Chemicals Pvt Ltd (1999 33 CLA 33 CLB) case, this Board has held that we have to examine whether the facts reflect the existence of any understanding of joint management justifying the claim of legitimate expectation of being an MD. Karnataka High Court also, in Synchron Machine Tools Pvt Ltd case, has recognized application of legitimate expectation in a petition under Sections 397/98.***”

“As held by this Board in Thirthram Ahuja's case (supra), when certain groups of shareholders who have formed a company and have been participating in the affairs of a company for a long time with remuneration, then there can be a presumption of legitimate expectation and exclusion of one from the management could be an act of oppression.”

Other cases

* *In re Astec (B.S.R.) Plc.* [1998] 2 B.C.L.C. 556, 588:

"in order to give rise to an equitable constraint based on 'legitimate expectation' what is required is a personal relationship or personal dealings of some kind between the party seeking to exercise the legal right and the party seeking to restrain such exercise, such as will affect the conscience of the former."

* *BSB Holdings Ltd. (No. 2) Re,* (1996) 1 BCLC 155 at 242 (Ch D)

Legitimate expectations may be superimposed in certain instances where it may arise from agreements between the members or between the members and the directors.