The separation of ownership and control and dispersal of shareholders all over the country make it of considerable importance to know the rights, privileges and liabilities of the shareholders. In the last few years, the role, functions, duties and rights of shareholders have been discussed quite frequently. It is felt that shareholders are not taking active interest in the working and management of companies. There are several matters where the management's decisions are to be approved by ordinary or special resolution under the Companies Act but the general meetings are not well attended. Recently, groups of shareholders in certain companies have fought their issues through wide publicity in the press. The shareholders' democracy has not yet become effective due to lack of vigorous and well developed shareholders' opinion in spite of about 200 provisions in the Companies Act relating to the rights of the shareholders.

John Galbraith in his book *The New Industrial State* has observed that "the annual meeting of the large American Corporation is perhaps our most elaborate exercise in popular illusion". The same applies with equal force in India. The shareholder in a large company does not feel like attending the general meetings as all the powers vest in the directors or controlling shareholders. He is only interested in the value of his shares and dividends. If he finds that he is not getting a good yield or there are no prospects of appreciation in the value of his shares, he changes his investment to shares of other companies. The present paper attempts to show the reforms desired to strengthen the position of the shareholders.

**Rights of Shareholders**

The rights of the shareholders may be broadly divided into three categories:

1. The rights of the individual shareholder,
2. The rights of the minority shareholders, and
3. The rights of the majority shareholders.

*B.A., F.C.A., J.P.*
An individual shareholder is entitled to get copies of the memorandum and articles of association, trust deed securing issue of debentures, register of members, minutes of the proceedings of general meetings, register of contracts, companies and firms in which directors are interested, contract or board resolution appointing manager, managing director, etc., registers of loans to companies under the same management, investments maintained under sections 372(9), 356, 358, 359 and 360. The Companies Act further gives a shareholder the right to inspect the register and index of members and debenture holders, annual returns, registers of investments, charges, contracts, directors, directors' shareholdings, loans to companies under the same management, investments in shares of other companies and the minute books of general meetings. However, a shareholder does not enjoy the right to inspect the books of account, the reason being that the interests of the company may suffer if important and vital information regarding the day-to-day working of the company is made available to the shareholders who may be competitors or may give out the information to rivals.

The right of inspection of books of account is available in certain States in the U.S.A., and in Japan to a specified number of shareholders. There appears to be no sound reason why in India also a respectable minority of ten per cent or so should not be provided the right of inspection of books of account. A person holding ten per cent of the equity paid up capital has got a reasonable stake and will not like to harm the interests of the company. The competitors have their own way of getting the information by 'commercial spying' and it should not be taken for granted that the person holding one-tenth of the shareholding can be easily influenced by the competitors to part with the information. The right to

1. Companies Act 1956, (hereinafter referred to CA) section 39(1).
2. CA section 118(1).
3. CA section 163(4).
4. CA section 196(2).
5. CA section 301(5).
6. CA section 302(6).
7. CA section 370(1F).
8. CA section 362.
9. CA section 163.
10. CA section 49.
11. CA section 144.
12. CA section 301(5).
13. CA section 304.
14. CA section 314.
15. CA section 370.
16. CA section 372.
17. CA section 196.
inspect books of account is an important method of obtaining useful information about a company by the shareholders so that they may take necessary action against the management for mismanaging the affairs of the company. Further, one-tenth of the shareholders can apply to the government for investigation under section 235 or may move the Court for relief against oppression or mismanagement under sections 397 and 398 but they cannot approach the authorities for taking action unless they have the means to obtain information. As a safeguard against misuse, the right may be granted subject to the approval of the Government who should be empowered to refuse the permission if the company is able to satisfy that the right is likely to be misused or that the shareholder is moved by improper motives.

Right of Shareholders to Receive Notice of Meetings

Notice of every meeting must be given to every shareholder either personally or by post at his registered address in India or if he has no registered address in India, to the address, if any, within India supplied by him to the company for giving notices to him. A notice calling a meeting must state the place, day and hour of the meeting and the statement of the business to be transacted thereat. The Calcutta High Court has held in Biswanath Prasad Khaitan v. New Central Jute Mills Company Limited that the notice convening an extraordinary general meeting must be fairly and intelligently framed and it must not be misleading or equivocal. A benevolent construction will not be applied in constructing a notice. Twenty one days' notice must be given for calling any kind of general meeting and for passing any kind of resolution, whether ordinary or special. A general meeting may be called by giving shorter notice if, in the case of an Annual General Meeting, all the members entitled to attend and vote agree to it in writing and in the case of other general meetings only when members holding 95 per cent of the total voting power agree to do so. The twenty one days length of notice has been fixed to provide time to the shareholders to organise themselves and canvass opinion on the agenda and resolutions to be considered at the general meeting. The right of the individual shareholder to receive the notice of twenty one days cannot be taken away by the majority of shareholders even by passing a special resolution. Even if it could be proved that a member would not have attended the meeting, that will not excuse the convener of the meeting from giving him proper notice.

Voting Rights

Every member of a company limited by shares and holding any equity share capital shall have a right to vote in respect of such capital

on every resolution placed before the company and his voting right on a
poll shall be proportionate to his share of the paid up equity capital of
the company. A member holding any preference share capital shall
have a right to vote only on resolutions which directly affect the rights
attached to preference shares. Every equity shareholder has a right to
vote upon such questions as the company is legally competent to deal
with even if he may have a personal interest in the subject-matter opposed
to or different from the general or particular interests of the company.
The shareholder's vote is a right to property and prima facie may be
exercised by a shareholder as he thinks fit in his own interest. If
a shareholder's name is entered in the register of shareholders of the
company, he cannot be prevented from enjoying the right to vote
on the ground that his name has not been on the register for
any specified period before the date of voting. A company cannot
by its articles of association or otherwise impose a restriction that a
shareholder holding less than a minimum number of shares shall not be
entitled to vote. However, section 181 permits a company to put
restrictions on the exercise of the voting right on two grounds, namely, (1)
non-payment of calls, or (2) when the company has any right of lien and
exercises it. A private company not a subsidiary of a public company is
exempted from the operation of section 182 and can, therefore, put
restrictions on the exercise of voting rights of members in its articles of
association in addition to the above grounds.

Prior to the Companies Act 1956, the persons who did not have
much financial interest in the company could control the voting rights and
dominate the affairs of the company by issuing and owning deferred or
founders' shares with disproportionate voting rights. The disproportionate
or excessive voting rights on share capital issued before the commencement
of the Companies Act 1956, have ceased to exist by the end of the year
after the commencement of the Act. The paid up capital of the company
is the pivot around which the voting rights revolve and as such no
artificial majority can be created by persons not having a financial stake
in the affairs of the company. The Act recognises two kinds of capital,
namely equity share capital and preference share capital. A private
company unless it is a subsidiary of a public company is, however, free

21. CA section 87(1).
22. CA section 87(2).
24. Imperial Chemical Industries Limited, In re. (1938)8 Comp. Cas. 181. Per Lord
Maugham.
"Madras 927.
26. CA section 182. See also Pasari Flour Mills Limited, In re. (1962) 32 Comp. Cas.
896.
Rights of Shareholders under the Companies Act

to issue shares of different kinds and with disproportionate voting rights and rights as to dividend and capital.

Right to Appoint Proxy

Section 176 gives a very important right to a shareholder, who is entitled to attend and vote at a meeting of the company, to appoint another person (whether a member or not) as his proxy to attend and vote instead of himself. It is not convenient for a shareholder generally to attend the meetings of a company situated at a far away place. But through the system of proxy he can make use of his right to vote by appointing a man of his choice as his proxy. The Companies Act prohibits the directors to canvass proxies at the expense of the company. It is obligatory on the part of a company to inform the shareholders of the right to appoint a proxy by giving in every notice calling a meeting of the company a statement or note with 'reasonable prominence' that a member entitled to attend and vote at a meeting of the company shall be entitled to appoint his proxy to attend and vote instead of himself and that the proxy need not be a member. If this information is omitted, every officer of the company who is in default is liable to a fine. This provision is not applicable to a private company unless it is a subsidiary of a public company and also to companies limited by guarantee not having a share capital unless their articles provide for proxy voting.

It is not permissible for a public company or a private company which is subsidiary of a public company to provide any stipulation requiring the lodging of proxy more than 48 hours before the meeting. If an instrument appointing a proxy is in any of the forms set out in Schedule IX, the company cannot question it on the ground that it fails to comply with any special requirements for such an instrument contained in the articles. A company cannot also refuse to accept the proxy merely because there is a minor mistake of misprint in it. The omission of the date of execution on the instruments of proxy is not a serious defect on which the proxy can be declared void. The company may supply to a member a form of proxy and a list of persons willing to act as proxies provided such a form and the list of persons are made available on request to every member, but the company cannot issue any invitation to members to appoint a named person as a proxy. If a member wants the proxy not to use his discretion but to vote in a particular manner, he may use the 'two way form' and strike out the words in favour of or against contained in the form, to cast his vote on the question at issue.

A proxy is not entitled to speak at the meeting. It, however, needs to be considered whether the proxy should be provided the right to speak.

in the meeting so that effective control may be exercised by the shareholders through their agents by asking pertinent questions on the working of the company or the adoption of any resolution. The shareholders in India are spread far and wide and it is not possible for them, particularly the ladies who are also shareholders, to attend the meetings of the companies. The reason for not allowing the proxy the right to speak at a meeting is that the same may be abused by some of the shareholders, who, out of malice or ulterior motives, may appoint certain undesirable persons as their mouthpieces for harassing the management. If a certain shareholder is determined to harass the management by asking questions and making impassioned speeches, he can easily get one share transferred in the name of his mouthpiece who will then be able to speak and vote. It does not seem convincing not to allow proxies to speak at the meetings.

Postal Voting

The resolutions are required to be passed at the general meeting of the shareholders and hence postal voting is not allowed. It should be considered whether postal voting should be allowed in India in the case of big public companies whose shareholdings are spread all over the country. Gower has very rightly said that, general referendum is by far the best method of obtaining the views of the members as a whole but the fiction is preserved that the result is determined after oral discussion at a meeting and by those present thereat although everyone knows that personal attendance is the exception rather than the rule and that the result is normally determined by proxies lodged before the meeting is even held.

Right of Proxy to Vote by Show of Hands

Voting at the general meetings is done by show of hands unless a poll is demanded. In the case of a vote by show of hands a member present by proxy has no right to vote. It is not a satisfactory position that the proxy is not entitled to vote on show of hands. The law, of course, permits that the articles may give this right but usually there is no practice to give the proxy the right to vote on a show of hands. The proxy should be given the statutory right to vote on show of hands as otherwise the result can never give a correct and true picture of the opinion of the members on any controversial resolution.

Demand for Poll

A poll may be demanded under section 179 by the following persons:

(a) In the case of a public company, by at least five members having the right to vote on the resolution and present in person or by proxy.

29. CA section 189.
30. GA section 177.
(b) In the case of private company, by one member having the right to vote on the resolution and present in person or by proxy if not more than seven members are personally present, and by two members present in person or by proxy if more than seven members are personally present.

(c) By any member or members present in person or by proxy and having not less than one-tenth of the total voting power in respect of the resolution, or

(d) By any member or members present in person or by proxy and holding shares in the company conferring a right to vote on the resolution being shares on which an aggregate sum has been paid which is not less than one-tenth of the total sum paid up on all the shares conferring that right.

It would appear from the above that a proxy may demand or may join in demanding a poll.

It is obligatory that if a poll is demanded on a question of adjournment, it shall be taken forthwith. If a poll is demanded on any other question, not being a question relating to the election of a Chairman which is provided for in section 175, the poll may be taken at any time as directed by the Chairman, but not later than 48 hours from the time the demand for the poll is made. Where a poll is taken, the meeting is regarded as continuing until the ascertainment of the result of the poll. Section 183 gives a member the right to use his votes differently on a poll. A member entitled to more than one vote or his proxy or other person entitled to vote for him as the case may be, need not, if he votes on a poll at a meeting of the company, use all his votes in the same way. A private company which is not a subsidiary of a public company is, however, not bound to follow the provisions of section 179 or 180 regarding the demand for a poll or time for taking a poll and may make its own provisions by articles in respect thereof as it may think fit.

Where a poll is to be taken, the Chairman of the meeting shall appoint two scrutinisers to scrutinise the votes given on the poll and to report to him. Of the two scrutinisers appointed, one shall have to be a member, not being an officer or employee of the company, present at the meeting provided that such a member is available and is willing to be appointed.

Right to Speak at a Meeting

A shareholder has a right to be heard at a meeting in reasonable terms and for a reasonable time. A company meeting is a privileged occasion and statements made thereat by a shareholder will not make him liable for defamation in the absence of malice.

Right of Appeal Against Refusal to Register Transfer of Shares

If a company refuses to register any transfer of shares or transmission of right, whether in pursuance of any power under its articles or otherwise, it shall within two months from the date on which the instrument of transfer or the intimation of such transmission as the case may be, was delivered to the company, send notices of the refusal to the transferee and the transferor or to the persons giving intimation of such transmission as the case may be. Section 111 gives the right to the transferor and the transferee or to the persons who gave intimation of the transmission by operation of law, as the case may be, where the company is a public company, or private company which is a subsidiary of a public company, to appeal to the Government against any refusal of the company to register the transfer or transmission or against failure on the part of the company to send notices of its refusal as mentioned above. The transferability of a share is a very important right to the shareholder of a public company as it adds to its negotiability and hence the right of appeal to the Government is an important safeguard against capricious and malafide refusal to register the transfer of shares. The alternative remedy against refusal to register the shares is to apply to the Court for rectification of the members' register.\(^32\) It was held by the Supreme Court in *Harinagar Sugar Mills Ltd., v. Shyam Sunder Jhunjhunwala*,\(^3\) that in an appeal under section 11(3) the dispute relates to the civil rights and in deciding the appeal the Government acts as a tribunal and not as an executive body. It has been held further in *Arjan Singh v. Panipat Woollen and General Mills Co. Ltd.*,\(^35\) that section 155 does not purport to confer over-riding powers on the Court and hence the Court will not entertain a petition where the aggrieved shareholder has availed of the alternative remedy under section 111 of the Act. However, an order passed by the Government under section 111 is appealable to the Supreme Court by special leave under article 136 of the Constitution.

Right to Apply to the Government to Call Annual General Meeting

If default is made in holding an Annual General Meeting in accordance with section 166, any member may apply to the Government under section 167, and the Government may give directions for calling, holding and conducting the meeting. The fact that the annual accounts of the company were not ready cannot be an excuse for not calling the Annual General Meeting.\(^36\) For failure to call the Annual General Meeting under section 168, the guilty directors can be held liable under

\(^{32}\) Hereinafter the Government means Central Government unless otherwise stated.

\(^{33}\) CA section 155.

\(^{34}\) (1961)31 *Comp. Cas.* 387.

\(^{35}\) (1963)33 *Comp. Cas.* 534.

\(^{36}\) *E.I. Sombrero Ltd., In re* (1958)28 *Comp. Cas.* 619.
section 210(5), in addition to their being convicted, for default in not placing before the Annual General Meeting the balance sheet and profit and loss account for the year concerned. An extraordinary general meeting convened in accordance with the requisition of the shareholders cannot be considered to be an 'annual general meeting'.

Any member of the company who is entitled to vote at the meeting has a right to apply to the Court under section 186 to direct the holding of a meeting other than an Annual General Meeting, if for any reasons it is contended that it is impracticable to hold the meeting. The mere fact that a member owes to the company a sum of money or that the company has a lien on his shares for his debts and engagements does not deprive the member of his right to be present at any general meeting or to vote therein and he can therefore present an application to the Court under section 186 for an order directing the calling of a meeting. The word 'impracticable' used in the section is more limited than the word 'impossible' and means impracticable from a reasonable point of view. If there is a serious doubt and controversy as to who are the directors and where there is a possibility that one or other or both the meetings called by the quarrelling groups of directors may be invalid, section 186 may be invoked.

Right to Convene Extraordinary General Meeting

A certain specified number of shareholders enjoy the right to convene an extraordinary general meeting of the company under section 169 of the Act. It is obligatory on the part of the directors to call an extraordinary general meeting on the valid requisition of holders of not less than one-tenth of the equity capital carrying voting rights. If the directors fail to call an extraordinary meeting within twenty one days from the date of the deposit of a valid requisition in regard to any matters for consideration on a day not later than 45 days from the date of deposit of the requisition, the meeting may be called by the requisitionists themselves or by such of the requisitionists as represent either a majority in value of the paid-up share capital held by all of them or not less than one-tenth of such of the paid-up share capital carrying a voting right, whichever is less. If the registered office of the company is locked up, the requisitionists can hold the meeting at some other place. The requisitionists are entitled to realise reasonable expenses incurred by them in calling such meeting and the company shall recover the same from the fees or other remuneration of the defaulting directors.

38. Supra note 26.
40. Raghunath Valusami Chettiar v. Manickavelu Chettiar and others, (1951)21 Comp. Cas. 93.
Legal Actions by Shareholders

Although a shareholder is bound to accept the decision of the majority by virtue of his contract with the company and other members, the individual member has got certain right such as the right to vote at the meeting, to speak at the meeting, to move an amendment to a resolution, to appoint proxy, to receive and sue for dividends which have been declared and such rights cannot be taken away by the majority action of the shareholders. According to the rule of law laid down in the well known case of Foss v. Harbottle, an individual shareholder cannot sue for a wrong done to the company except in certain circumstances.

The reasons for this rule may be summarised below:

1. The proper plaintiff in an action in respect of a wrong alleged to be done to a company is prima facie the company itself.
2. If the irregularity complained of is a transaction which can be effectively rectified by a simple majority of the members, there is no use of litigation.
3. If each shareholder is permitted to sue the company, the company would be harassed by a multiplicity of suits.

The rule in Foss v. Harbottle, greatly strengthened the position of the majority. However, due to the separation of control and ownership and the development of the concept of modern corporation, certain exceptions have been recognised by subsequent judicial decisions and an individual shareholder is allowed to sue in the following cases:

1. Where the legal action is to restrain the directors from committing an ultra vires or illegal act.
2. Where the act complained of is a fraud against the minority and/or is a failure on the part of the majority to act bona fide in the best interests of the company.
3. Where the shareholder seeks to restrain the company from acting on a resolution which has been passed by a simple majority when it should have been passed by a qualified majority, i.e., as a special resolution.
4. Where the directors are acting in contravention of the Companies Act or the Articles of the company.
5. Where the shareholder complains that his personal rights as shareholder have been infringed or may be infringed.
6. Where the shareholder submits that in the interest of the justice, the procedural rule requiring a suit by the company should be disregarded.

41. (1843) 2 Hare. 461.
Foss v. Harbottle laid more emphasis on the procedural character of the action, based on the reason that a company is a separate legal entity and if it sustains a legal injury, it does not follow that all the members individually suffer legal injury too. The exceptions given to the shareholders to file a suit on behalf of the company is that where the persons in control of the company do not take steps to enforce the rights of the company, the shareholders as representatives of the company are allowed to sue. Pennington in his book *Company Law* has described such individual member's action as "derivative action" as the right to sue is derived from the company. The company, however, must be made a defendant in the action as the money recovered will be in favour of the company.

Compulsory Audit—Safeguard to Shareholders

The provisions of compulsory audit of the companies by chartered accountants is a great safeguard for the shareholders. The auditors have to examine the accounts and certify that the profit and loss account gives a true and accurate view of the profit or loss of the year and the balance sheet gives a true and accurate view of the state of affairs of the company. The auditors of the company are also required to state in their report whether in their opinion proper books of account as required by law have been kept. The auditors can be held liable if they have failed in their duties to carry out the audit properly and report to the shareholders faithfully. The Institute of Chartered Accountants of India takes a very serious view of the failure of the duty of chartered accountants and ensures, by taking appropriate action against erring members, a high standard of audit. It is due to the faith in the integrity of chartered accountants that a demand is being made in certain quarters that the scope of normal statutory audit should be enlarged and auditors should be called upon to express their opinion on the propriety of the transactions also, so that the shareholders' interests may be served better.

Importance of Directors' Report

Prior to the Companies Act 1956, the directors' report sent to the shareholders was in most cases a skeletal document giving little information about the working of the company. The preparation of directors' report depends to a large extent on the initiative and judgment of the directors. Section 217 has made it obligatory for the directors to give information as to the state of the company's affairs and to set out the material changes and commitments, if any, affecting the financial position of the company which have occurred between the end of the financial year of the company to which the balance sheet relates and the date of the report.

The report must also contain the information in respect of the sums, if any, which the board proposes to carry to any reserves and the sum
which the board recommends for being paid by way of dividend. The board is bound to give full information and explanations in its report on every reservation, qualification or adverse remark contained in the auditors' report.

The directors, at present, are not bound to give reasons in the board report regarding the non-declaration of dividends, even where the profits of the company are sufficient to declare the dividend. It should be made compulsory on the part of directors, where no dividend has been declared in spite of sufficient profits, to give the reasons for ploughing back the profits and to annex a statement explaining the uses of such funds. There should also be a provision in the Act for issuing half-yearly working report by the directors so that the shareholders are posted with the latest developments in the company. This will create confidence in the investors and will help in the growth of the corporate sector.

Utility of Unit-wise Accounts

It is not obligatory on the part of a company dealing in various kinds of business activities to prepare a unit-wise profit and loss account or balance sheet. Many companies are doing different types of businesses such as sugar, chemicals, cement, fertilisers etc., but are not publishing units-wise accounts of such distinct business activities. The result is that the shareholders are not in a position to know whether a particular business activity is profitable or not. These units claim themselves as independent industrial undertakings before income-tax authorities for the purposes of getting benefit of tax holiday as per section 84 of the Income-tax Act. These companies maintain separate books of account for each unit and also file profit and loss account of each unit with the income-tax authorities for claiming tax benefit. Some of the companies publish unit-wise accounts but a majority of such companies do not do so. It is, therefore, necessary to consider whether any provision should be made in the Companies Act requiring such companies to publish unit-wise account. The legislation may create certain difficulties for companies. The rigid definition of a 'unit' may create hardship for the companies in the maintenance of independent accounts for each unit and add to their cost. There are bound to be certain common overhead expenses and allocation of such expenses between different units may also cause difficulty. The question is, how long, the shareholders can be denied the information regarding the working result of the various units. It may be argued that such compulsory provision does not exist even in advanced countries of the world. But the companies in such advanced countries give a lot of information to the shareholders. In America the companies give many types of charts and statements such as statement of surplus, financial information dealing with events such as revaluation, written-off debts, discounts and exchanges in surplus, progress report, statement showing
why no dividend has been declared. Some of the progressive companies in India are also giving a lot of meaningful information which is not required by law. The rest of the companies should also start publishing unit-wise accounts, wherever practicable, so that legal compulsion may not be necessary.

**Disclosure of Material Facts**

The compulsory disclosure of material facts in respect of certain resolutions is a method of giving important information to the shareholder so that they may appraise the soundness of the proposal on which they are asked to vote. According to section 173, if any item of business to be transacted at a meeting is deemed special, the directors must explain the reasons for the proposed resolution in an explanatory statement to be annexed to the notice setting out all material facts regarding it and the nature of the concern or interest, if any, of every director and manager.

The proceedings at the meeting may be declared invalid for insufficient disclosure in the notice. It has been held that if the directors want the sanction of the shareholders, they must give a fair, reasonable and full statement of the facts upon which they are asking the shareholders to vote. If there is a large body of shareholders who reside at long distances from the registered office of the company, it is not enough on the part of the company to keep available for inspection a copy of the proposed resolutions at the registered office and merely give the shareholders notice of the fact that a copy of the proposed resolution will be available for inspection at the registered office of the company.

**Right to Get Company’s Affairs Investigated**

A specified number of shareholders have got the right to get the affairs of the company investigated through the Government under section 235 of the Act. In the case of a company having a share capital, two hundred members or members holding not less than one-tenth of the total voting power, or, in the case of a company not having a share capital, one-fifth number of persons on the company’s register of members may request the Government to appoint inspector or inspectors to investigate the affairs of the company. Such minority shareholders will, however, have to satisfy the Government that they have good reasons for requiring the investigation. Since the shareholders have got no right to inspect the books of account, it is difficult for them to furnish satisfactory evidence in support of their petition. But if _prima facie_ the Government feels that the allegations have some force, they may collect facts before ordering investigation by surprise inspection of books of account under section 209 of the Act without any stigma of investigation harmful to the company.

42. Bimal Singh Kothari _v._ Muir Mills Company Limited, (1952)22 Comp. Cas. 248.
It needs to be considered whether it should be made mandatory on the part of the Government to order investigation if requested by over 200 members or holders of twenty per cent of the issued shares unless it considers that the application is vexatious, and made out of malice. However, the wide powers given to the Government under section 237 of the Act are a great safeguard to the shareholders against abuses and malpractices by the management. It is incumbent on the part of the Government to appoint an inspector to investigate the affairs of a company where a demand is made by the shareholders by passing a special resolution or where the Court by order declares that the affairs of a company ought to be investigated by an inspector appointed by the Government. The Government has further powers to order investigation if in its opinion, there are circumstances suggesting:

(i) that the business of the company is being conducted with intent to defraud its members, creditors or otherwise for a fraudulent or unlawful purpose,

(ii) that persons concerned with management are guilty of fraud, misfeasance or other misconduct towards the company or its members,

(iii) that the members of the company have not been given all the information with regard to its affairs which they might reasonably expect.

The shareholders can persuade the Government under this section to order investigation by pointing out the areas of malpractices even if they have no positive proof.

In fact, the Government has used this power in a number of cases. However, the Supreme Court has held that although formation of opinion by the Government under section 237 is a purely subjective process, the expression 'circumstances suggesting' points out that there must exist circumstances from which the government forms an opinion and if it is shown that the circumstances do not exist or that they are such that it is impossible for any one to form an opinion therefrom suggestive of the aforesaid things, the opinion is challengeable. It further held that the existence of circumstances has to be proved at least prima facie. The Government has powers under section 247 to investigate as to who are the persons financially interested in the success or failure of the company or who control or materially influence the policy of the company. It may be said in the words of Gower that the Government has ceased to be a merely vigilant onlooker and has become a watch-dog with sharp teeth.

Protection of Minority Shareholders

Although the corporate action is governed by the rule of majority, it has been recognised that the majority should not be allowed to act in a manner fraudulent, oppressive or unfair to the interests of the company or the minority shareholders. There are certain rights enjoyed by individual shareholders which cannot be bypassed by the majority action. No shareholder can be compelled, by making any alteration in the Memorandum and Articles of Association after the date on which he became a member, to take or to subscribe for more shares than the number held by him at the date on which the alteration is made, or which in any way increases his liability to contribute to the share capital or otherwise pay money to the company.

Pre-emptive Right of Minority Shareholders

Section 81 of the Companies Act gives a very important right to the minority shareholders of a public company to participate in the further issue of shares in proportion to their existing shareholdings so that the minority cannot be frozen out or reduced to a relatively insignificant voting power. The directors are required to offer the new issue of shares first to the existing shareholders before issuing it to outsiders. The directors can issue further shares to outsiders only with the consent of a special resolution or by an ordinary resolution with the permission of the Government. The requirement of a special resolution is not sufficient as there is a scope for the majority of seventy-five per cent to freeze out the minority. As a safeguard to the interests of the minority shareholders, the sanction of the Government should be made compulsory, even where shares are offered to outsiders with the sanction of a special resolution so that the matter may be screened by the Government in the interest of the company by hearing the dissenting shareholders. It is possible for the majority of seventy-five per cent to decide to exclude the existing shareholders and then allot the new shares to outsiders who may in reality be the nominees of the majority. The usual ground for issuing the shares to outsiders is that the company requires money for expansion. If some of the shareholders are in a position to make an additional contribution of capital, majority should not be allowed to curtail the pre-emptive rights of the minority shareholders. A similar situation arose in Shantiprosad Jain v. Kalinga Tubes Limited, where the minority was willing to contribute but the majority shareholders decided to offer the additional capital to outsiders and not to the existing shareholders. The Supreme Court held that the majority shareholders were not bound to accept the view of the minority shareholders that the new shares should be allotted only to the existing shareholders. The mere fact that the majority shareholders decided to offer the new shares to others and not to the existing shareholders.

44. [1965]35 Comp. Cas. 351.
shareholders could hardly be said to be oppressive of the minority shareholders. The minority shareholders in this case could not prove that the new allottees were mere benamidars or stooges of the majority group and that the majority had a desire to oppress the minority. It further observed that the fact that the majority group might be able to get the support of the new shareholders did not necessarily mean oppression of the minority nor was the fact that the shares were issued to the friends of the majority group of any significance in the matter of oppression, for if shares were issued privately, they were bound to go to the friends of the directors and that the haste in issuing the new shares could not be said to be a part of the design to oppress the minority.

It may be noted that the pre-emptive right is not available to shareholders where the capital of the company is increased by the conversion of debentures and loans into shares as per the exercise of option given in the loan agreement or debentures instrument and the terms are approved by special resolution of the company and by the Government.

If there is oppression of the minority of shareholders and mismanagement, a minimum of one hundred members or members holding not less than one-tenth voting power may petition the Court under section 397 and 398 or as an alternative remedy may apply to the Government under section 408. The Government may also authorise any member or members if in its opinion circumstances exist which make it just and equitable to do so. The preference shareholders may also join in the petition. A member may apply to the court in a representative capacity by obtaining the consent of the requisite number of members in writing.

An order under section 397 granting relief against oppression will be made by the Court only if it is satisfied that the affairs of the company are being conducted in a manner oppressive to any member or members, and secondly, that the facts of the case are such that it would be 'just and equitable' to make an order for winding up of the company but the making of such an order would unfairly prejudice the members. Further, it has been laid down by the Supreme Court in Shriji Prasad Jain's case that there must be a continuous course of conduct which involves at least an element of lack of probity or fair dealing continuing up to the date of petition and not merely an isolated act of impropriety to bring the case within the ambit of this section as the words 'are being conducted' implies a continuity of wrongful acts. Further the oppression must be such that it would be just and equitable to wind up the company. The purpose and object of the section is to provide an alternative remedy to a petition for winding up by putting an end promptly and speedily to acts of oppression and mismanagement, it is submitted that the Companies Act should be amended to make it clear that oppression means isolated acts as well as a course of misconduct. The expression 'just and equitable to wind up'
should be deleted from this section thereby breaking the link with winding up so that all that would have to be proved would be 'oppression' in the wider sense. Every member of the company is entitled to have the affairs of the company conducted fairly, properly, regularly and according to law and therefore it does not seem proper why the power to approach the Court should not be given to every member instead of allowing it to a specified number of shareholders only.

The Courts have been given wide powers under section 402 to deal with the petitions under section 397 and 398 to award compensation to shareholders who have been oppressed to remove the directors and other managerial personnel and order the appointment of directors on the principle of proportional representation and may provide for the regulation of the conduct of the company's affairs.

The Government has also been vested with the powers under section 408 to prevent mismanagement or oppression. The Government can appoint two persons as directors to hold office for a period not exceeding three years or may direct the company to provide for proportional representation for appointment of directors by amending the articles of association of the company. The Government can also prevent changes in the board of directors likely to affect the company prejudicially.

Representation of Minority Interests on the Board

Section 255 of the Companies Act allows a company to adopt proportional representation whereby the minority shareholders may look for a chance of representation on the board, but in actual practice only a microscopic minority of the companies have adopted it. The proportional representation was not made compulsory for the companies as it was felt that the Board of Directors may become a contesting field for warring factions of shareholders and the smooth working of the company may be rendered virtually impossible. It is now being felt that the option given to the companies to adopt proportional representation for appointment of directors has no value. Unless a respectable minority of the shareholders are allowed some right of representation on the Board, they cannot know about the real state of affairs. Compulsory provisions to elect directors by the method of proportional representation or cumulative voting exist in a number of States in the U.S.A. It is to be considered whether the system of proportional representation should be made compulsory in India. The High Courts have powers to force cumulative voting upon a company if they find that the minority is oppressed under a system of straight voting. The Government also has powers under section 403 to direct the company to amend its articles and to make appointments of directors according to proportional representation to prevent mismanagement and oppression of members. However, such appointments by the order of a Court or of the Government are only possible in certain exceptional cases.
and cannot be treated as a substitute for the right to seek representation on the board by the minority shareholders. In fact, the Government has used these powers very sparingly and has preferred to appoint non-members instead of shareholders as directors under sub-section (1) of section 408.

Rights of Dissenting Shareholders and the Appraisal Remedy

If the rights attached to any class of shares are varied, the shareholders holding not less than ten per cent of the issued shares of that class who did not consent and/or vote in favour of the resolution for the variation, may apply to the Court under section 107 to have the variation cancelled. Where any such application is made, the variation shall not have effect unless confirmed by the Court. The Court may after hearing the applicant and any other persons who apply to the Court to be heard and appear to the Court to be interested in the application, may, if it is satisfied that the variation would unfairly prejudice the shareholders of the class represented by the applicant, disallow the variation. Where there is a contract or a scheme involving the transfer of shares to another company approved by nine-tenth of the shareholders under section 391, the dissentient shareholders may go to the Court for relief. This is called the Appraisal Remedy in the U.S.A. as it enables the minority to have their shares sold at a fair price. This is an important safeguard to the minority shareholders against the majority. However, unless there is unfair dealing to the minorities, the minorities are made to fall in line with the majority by Courts as the minority cannot be allowed to act unreasonably.

Requirement of passing a Special Resolution

The requirement of getting the sanction of shareholders by special resolution in many important matters is a great safeguard to the interests of minority shareholders. The votes cast in favour of a special resolution, whether on a show of hands or on poll by the members entitled to vote, must be at least three times the number of votes cast against the resolution. The shareholders must be informed in the notice calling the general meeting or otherwise of the intention to propose the resolution as a special resolution. The directors must disclose all material facts necessary for the purpose of passing the special resolution in the explanatory statement. A special resolution is required for many matters such as to alter the provisions of the memorandum of association, to commence any new business, to offer a further issue of shares to outsiders, to reduce the share capital, to keep registers and documents at any other

45. CA section 17.
46. CA section 149(2A).
47. CA section 81.
48. CA section 100.
place within the city other than the registered office, to pay interest out of the capital, to allow the holding of an office of profit by the directors or their relatives etc., to authorise remuneration by way of commission to a director who is neither in the whole-time employment of the company nor a managing director, to 'give loans to companies under the same management, etc.

It is usually seen that special resolutions are also passed without much discussion and deliberations. Although the special resolution require three-fourth majority of votes but as most of the members do not attend or even use their right to appoint proxies, the passing of the special resolution does not really reflect the wishes of the three-fourth majority of shareholders on the register of members but of only those present in the meeting by person or proxy. It is, therefore, desirable that to enable the majority of shareholders to exercise their judgment, postal voting as suggested earlier should at least be permitted in case of special resolutions.

A special resolution cannot be normally amended and must be voted upon in the exact form in which it appears in the notice. However, if a special resolution is framed in such a way that it gives possible indication of modification by using the words 'to pass it with such modification as thought fit', the widely held view is that an amendment may be moved to the special resolution by a shareholder. The amendment must, however, be germane to the subject-matter and should not go beyond the material facts set out in the explanatory statement or the scope of the original resolution.

**Right of Majority Shareholders to Remove Directors**

The shareholders have a right to remove, by an ordinary resolution, a director with whom they are dissatisfied before the expiry of the period of his office, except in the following cases:

(a) Where a director has been appointed by the Government in pursuance of section 408.

(b) In the case of a private company, if the director holds office for life on April 1, 1952.

(c) Where the company has availed itself of the option given to it under section 265 to appoint not less than two-thirds of the total number of directors according to the principle of proportional representation.

49. CA section 163.
50. CA section 208.
51. CA section 314.
52. CA section 309(4).
53. CA section 370.
Exercise of Power by Shareholders in General Meeting

The board of directors is usually vested with all the powers of management by the articles of association of the company. Section 293 provides certain restrictions on such powers. The directors cannot, except with the consent of the company in general meeting, sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company or, where the company owns more than one undertaking, the whole or substantially the whole of any such undertaking; remit or give time for the repayment of any debt due from a director; invest otherwise than in trust securities the amount of compensation received by the company in respect of compulsory acquisition; borrow money exceeding the paid up capital and free reserves of the company; and contribute to charitable and other funds not directly relating to the business of the company or the welfare of its employees any amount exceeding twenty five thousand rupees or five per cent of its average net profits during the three financial years immediately preceding, whichever is greater. If the shareholders want to retain more powers in their hands, they can amend the articles and usurp more powers for themselves. The power of the directors to recommend a dividend or to declare an interim dividend is exclusive and the members cannot resolve that larger dividends shall be paid to them than those decided by the directors.

The Controlling Shareholders

A ninety per cent majority of the shareholders is in a position to compel the ten per cent dissentient shareholders to sell out their shares. The majority of shareholders who control the board of directors can also compel the minority shareholders to sell their shareholdings by not declaring dividends in spite of good profits in the company. It is therefore necessary to consider how the controlling shareholders may be made to act in the bona fide interest of the company as well as the other minority shareholders. The controlling shareholders unlike the directors do not stand in any fiduciary relationship and are therefore not required to act in good faith in the interest of others. The controlling shareholders, it appears, are not liable to account to the other shareholders for the larger price obtained by them on sale of the block of their shares than that which the other shareholders have obtained in a take-over bid, although there are provisions in the Companies Act for making the directors responsible for it. It is submitted that the controlling shareholders should be obliged to account for such profit. Such provisions exist in the U.S.A. It has been held in a number of decisions of various American courts that the controlling shareholders are liable to account to the other shareholders.

Conclusions:

1. A right of inspection should be given to the shareholders to
inspect the books of account, in the present phase of development of the country.

2. An obligation should be imposed on the directors to give reasons in the board report regarding the non-declaration of dividends where the profits of the company are sufficient for guaranteeing declaration of dividends.

3. Responsibility should be laid down for issuing half-yearly progress reports of the companies and for publishing unit-wise profit and loss Accounts.

4. (a) A proxy should be given the right to speak at the meetings considering the socio-economic conditions of India.

(b) Postal voting should be permitted in the case of big companies whose shareholding is spread far and wide.

(c) A proxy should be entitled to vote on a show of hands.

5. Duties and obligations of the controlling shareholders should be specifically laid down.

6. The representation of a specified minority should be made compulsory on the Board of Directors.

7. The denial of the pre-emptive right to the minority shareholders by a special resolution should be made effective subject to the approval of the Government to avoid freezing out the interest of the minority shareholders.

8. Sections 397 and 398 of the Companies Act should be amended to make it clear that oppression covers isolated acts of oppression also and to delete the expression ‘just and equitable to wind up’ from section 397 and thus delink it from ‘winding up’ and make this alternative remedy effective against oppression and mismanagement as well.