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THE SUPREME COURT'S VERDICT ON THE DISPUTE BETWEEN THE TATAS AND CYRUS MISTRY

Background:

On, 8th November, 1917, Tata Sons was incorporated as a Private Limited Company. Subsequently, two companies, Cyrus Investments Private Limited and Sterling Investment Corporation Private Limited ("**complainant companies**"), forming part of the Shapoorji Pallonji Group ("**SP Group**"), acquired shares of Tata Sons. The shareholding of the SP Group has grown to 18.37% over the years. In August 2006, Mr. Cyrus Pallonji Mistry ("**CPM**") representative of the SP Group, was appointed as a Non-Executive Director on the Board of Tata Sons. Subsequently, he was also appointed as the Executive Deputy Chairman in the year 2012 for a period of five years until March 2017.

In October 2016, by a resolution of the Board of Directors, CPM was replaced with Mr. Ratan N. Tata ("**RNT**") as the Interim Executive Chairman. However, CPM continued to be the Non-Executive Director of Tata Sons. This acted as the trigger point for CPM, to launch an offensive. On the very next day, CPM wrote a mail alleging total lack of corporate governance and failure on the part of the directors to discharge their fiduciary duties. Though this mail was labelled as 'confidential', a copy of the mail landed up with the media. Due to this development, by separate resolutions passed at the meetings of the shareholders of Tata Industries Limited, Tata Consultancy Services Limited and Tata Teleservices Limited, CPM was removed from the Directorship of these companies. CPM then resigned from the Directorship of a few other operating companies of the Tata Group on gaining knowledge that there were impending resolutions to remove him from Directorship.

The complainant companies in which CPM holds a controlling interest, filed a company petition before the National Company Law Tribunal, Mumbai Bench ("**NCLT**") under Sections 241 and 244 of the Companies Act, 2013 ("**said Act**") alleging unfair prejudice, oppression and mismanagement by the majority shareholders.

The complainant companies, however, only had 2% of the total issued share capital of Tata Sons, thereby failing to meet the threshold of 10% required to file a petition under the said sections, alleging mismanagement and oppression.

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To seek an exemption from this requirement, an application was filed for waiver by the complainant companies. Along with this application, the complainant companies moved an application for stay of the Extra-ordinary General Meeting of Tata Sons in which a proposal for removing CPM as a Director of Tata Sons was to be placed. The stay was refused by NCLT and CPM was removed from the Directorship of Tata Sons by a resolution dated 16th February, 2017. NCLT also passed orders dated 6th March, 2017 and 17th April, 2017 holding the company petition as not maintainable at the instance of persons holding just 2% of the issued share capital and dismissing the waiver application, respectively. Appeals were filed with the National Company Law Appellate Tribunal ("**NCLAT**") against these orders which were admitted, and the matter was remanded back to the NCLT for disposal on merits.

The NCLT accordingly heard the company petition on merits and dismissed the same by an Order of 9th July, 2018 as below:

a. Rejection of petition to reinstate CPM on Tata Sons Board.
b. Dismissal of the application for waiver of the threshold requirement under Sections 241 and 244 of the said Act.
c. Refusal of stay of the EGM of Tata Sons.

Challenging the order of the NCLT, the complainant companies filed an appeal with the NCLAT, while CPM filed another cross appeal. Both the appeals were allowed. The NCLAT ruled in favour of the complainant companies and pronounced as below:

a. Restoration of CPM as Executive Chairman of Tata Sons.
b. Direction to Tata Sons to consult SP Group for all future appointments of Executive Chairman or Director.
c. Direction to Registrar of Companies to record Tata Sons as a Public Company.
d. Restraining the invocation of Article 75 of the Articles of Association, except in exceptional circumstances.

The final order of the NCLAT was challenged by Tata Sons before the Hon'ble Supreme Court of India ("**Supreme Court**"). RNT and the trustees of the two Tata Trusts filed two independent appeals challenging the order of the NCLAT. The grievance of RNT and trustees was with regards to the injunctive order of NCLAT restraining them from taking any decisions, without consulting the SP Group.

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Three operating companies of the Tata Group filed separate appeals and their grievance was with regard to CPM being reinstated as a Director of these companies for the rest of the tenure. The original complainants being the complainant companies filed a cross appeal before the Supreme Court and sought additional reliefs to provide them proportionate representation on the Board of Tata Sons and in all committees formed by the Board of Directors.

Issues before the Hon'ble Supreme Court:

The judgement pronounced by the three Hon'ble Judges, Justice S.A. Bobde, Justice A.S. Boppana and Justice V. Ramasubramanian, highlighted the important aspects of the Companies Act and its subsequent evolution over the years.

The Supreme Court framed five questions of law to be determined before determining the present case. A summary of these five questions framed by the Supreme Court is given below:

1. ***The first question has been divided into two parts:***
   a. Whether the removal of CPM could have been the basis for the allegations that the company's affairs have been or are being conducted in a manner oppressive or prejudicial?
   b. Whether the findings recorded by NCLAT about the existence of just and equitable grounds for winding up are in accordance with the well-established principles of law?

2. ***The second question has been divided into two parts:***
   a. Whether the reliefs granted and directions issued by NCLAT, including the reinstatement of CPM into Board of Tata Sons and other Tata Companies, was in consonance with the powers available under Section 242(2) of the said Act?
   b. Whether the relief relating to Article 75 of the Articles of Association was valid?

3. ***Whether NCLAT could have, in law, muted the power under Article 75 by simply injuncting the company from exercising such a right without even setting aside the said Article?***

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4. ***The fourth question has been divided into two parts:***

a. Whether the constant change in stand of the affirmative voting rights under Article 121A of the Articles of Association was proper?

b. Whether the claim of proportionate representation by SP Group on the board of Tata Sons is valid?

5. ***Whether there existed any illegality in re-conversion of Tata Sons from a public company into private company?***

Analysis:

The answers to these questions framed were discussed in great detail and the judgement was pronounced on the following findings on these five issues by the Supreme Court:

1a. Removal of CPM

- Supreme Court took note of the fact that at the time of filing of the original company petition by the SP Group, CPM was removed from his position of Executive Chairman while he continued to be the Director. This removal acted as a trigger point for CPM, as on the very next day of his removal, he wrote an email alleging total lack of corporate governance on the part of directors to discharge their fiduciary duties. It is noted that even though the mail was labelled as '*confidential*', the mail was leaked to the media, creating a sensation.

- On the allegation that the removal of CPM was oppressive, the Supreme Court observed the irony that although CPM's holding was of only 18.37% shares, yet he was identified as the successor to the empire, who now chose to accuse the same Board. Furthermore, the Supreme Court observed that failed business decisions and removal of a person can never be projected as acts oppressive or prejudicial to the interests of minorities.

- Thus, it was concluded by the Supreme Court, that, in a petition under Section 241, the Tribunal cannot ask the question whether the removal of a Director was legally valid and/or justified or not. The question to be asked is whether such a removal tantamounted to a conduct oppressive or prejudicial to some members. "Even in cases where the Tribunal finds that the removal of a Director was not in accordance with law or was not justified on facts, the Tribunal cannot grant a relief under Section 242 unless the removal was oppressive or prejudicial."

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- The Supreme Court noted that there may be cases where the removal of the Director might have been carried out perfectly in accordance with law and yet may be part of a larger design to oppress or prejudice the interest of some members. It is only in such cases that the Tribunal can grant a relief under Section 242.

- The Supreme Court hence held that removal of a person from the post of Executive Chairman cannot be termed as oppressive or prejudicial, as in the present case.

- The Supreme Court while answering this question also observed that NCLAT, being an Appellate Tribunal, conferred with the power to confirm, modify or set aside the order of NCLT, can be taken to be a final court of fact. An appeal from the Order of the NCLAT to the Supreme Court under Section 423 of the said Act is only on a question of law. Considering the nature of the jurisdiction conferred upon NCLAT, it is clear that the findings of the NCLT, not specifically modified or set aside by NCLAT should be taken to have reached finality, unless the parties aggrieved by such non-interference by NCLAT have approached the Supreme Court, raising this as an issue.

1b. Invocation of Just and Equitable clause

- A necessary condition precedent to grant of reliefs in an oppression and mismanagement case is that the Court must find that it is just and equitable to wind up the company. The NCLAT did not provide any factual foundations to justify such finding.

  The legal test applied here was laid down by the Privy Council in *Loch v. John Blackwood, "there must lie a justifiable lack of confidence in the conduct and management of the company's affairs, at the foundation of applications for winding up."* The Supreme Court observed that if this test was applied, the case on hand would not fall anywhere near the just and equitable standard, for the simple reason "*that the representative of the same complaining minority was not only given a berth on the Board but was also projected as the successor to the Office of Chairman*".

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- The Supreme Court while dealing with this issue also relied upon a few Indian cases being *Rajahmundry Electric Supply Corporation Ltd. v. Nageshwara Rao* wherein it was held that for the invocation of just and equitable clause, there must be a justifiable lack of confidence on the conduct of the directors. Further, in the case of *S.P. Jain v. Kalinga Tubes Ltd*., it was held that a mere lack of confidence between the majority shareholders and minority shareholders would not be sufficient.
- The Supreme Court observed that the present case did not fall anywhere near the just and equitable standard for the simple reason that it was the very same complaining minority whose representative was not merely given a berth on the Board but was also projected as the successor of the Office of the Chairman.
- The Supreme Court hence held that the NCLAT should have taken into account the nature of the company that Tata Sons is, a charitable trust, the dividends of which find their way eventually to the fulfillment of charitable purposes. The NCLAT should have raised a fundamental question of whether it would be equitable to wind up the company and starve to death those charitable trusts especially on the basis of "uncharitable" allegations of oppressive and prejudicial conduct. The finding of the NCLAT that the facts justified a winding up of the company under the just and equitable clause, is completely flawed.

2a. Reinstatement of CPM

- It was observed that CPM never prayed for his reinstatement either as a Director or as an Executive Chairman before the NCLAT. However, the NCLAT directed his restoration for the '*remaining tenure*'. While granting much more than what the complainant companies and CPM themselves thought as legally feasible, it was also observed that the '*remaining tenure*' of restoration had already run its course on the day of the NCLAT's judgement. The NCLAT granted the said relief of reinstatement gratis without any foundation in pleadings, without any prayer and without any basis in law.
  The Supreme Court observed that, a dismissal even if found to be wrongful and *malafide* is an effective dismissal and may give rise to a claim in damages, while citing the Hon'ble Court's judgement in *Dr. S.B. Dutt vs. University of Delhi*. It further observed that Sections 241 and 242 of the said Act do not specifically confer the power of reinstatement and that there is no scope for holding that such a power to reinstate can be implied or inferred from any of the powers specifically conferred.

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- The Supreme Court further held that the architecture of Sections 241 and 242 does not permit the Tribunal to read into the sections a power to make an order (for reinstatement) which is barred by law vide Section 14 of the Specific Relief Act, 1963 with or without the amendment in 2018. The Tribunal cannot make an order enforcing a contract which is dependent on personal qualifications such as those mentioned in Section 149(6) of the said Act. It further observed that "*the position in law that a contract of personal services cannot be enforced by Court is a long-standing principle of law and cannot be displaced by the existence of any implied power, though none is shown in the present case. This is described as the Principle of Legality.*

2b. Relief relating to Article 75

- Article 75 of the Articles of Association is about the company's power of transfer. The company through this Article may at any time by special resolution resolve that any holder of ordinary shares to transfer their ordinary shares.

- The Supreme Court observed that the relief could not have been technically granted by the NCLAT as the original petition had no prayers challenging Article 75. It was introduced only through subsequent amendment application. Moreover, there appears to be no instance of invocation of Article 75, or its misuse averred in the company petition or in the application for amendment. Thus, even if the application for Article 75 were to be considered, the NCLAT could not have made Article 75 completely ineffective by passing an order of restraint.

- Tracing the history of the evolution of the various Acts in relation to the provisions of Section 242 (1) of the said Act, the Supreme Court observed that despite the law relating to oppression and mismanagement undergoing several changes, the object that a Tribunal should keep in mind whilst passing an order in an application complaining of oppression and mismanagement is that the Tribunal should, by its order *"bring to an end the matters complained of"* and the NCLAT therefore could not have granted the said reliefs of (i) reinstatement of CPM (ii) restriction on the right to invoke Article 75 (iii) restraining RNT and Nominee Directors from taking decisions in advance and (iv) setting aside the conversion of Tata Sons into a private company.

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3. Power muted under Article 75

- The Supreme Court noted that Section 241(1)(a) provides for a remedy, only in respect of past and present conduct or past and present continuous conduct. The NCLAT has stretched the provision to cover the likelihood of a future bad conduct. The power exercised by the NCLAT to neutralize Article 75 merely on the basis of likelihood of misuse was observed to be impermissible by law.

- Article 75 of the Articles of Association was not an invention of the recent origin in Tata Sons. It has been there for nearly a century in one form or the other. The Supreme Court noted that SP Group willingly became a shareholder and thereby subscribed to the Articles of Association while also consenting to the amendments carried later. It observed that it is absurd for someone to turn around and challenge such Articles which were present since the inception.

- The Supreme Court noted that though the Tribunal has the power under Section 242 to set aside any amendment to the Articles that takes away recognized proprietary rights of shareholders, but the same is based on the premise that the bringing up of the amendment itself was a conduct that was oppressive or prejudicial. Thus, Supreme Court held the order of the NCLAT tinkering with the power available under Article 75 as wholly unsustainable.

4a. Affirmative Voting Right

- On the question of affirmative voting rights, the Supreme Court calls SP Group's position as "*rather funny*". It was noted that SP Group sought a prayer for striking off Article 121 in its entirety which was later amended to delete "the necessity of affirmative voting rights". Eventually, SP Group seemed to be fine with the existence of affirmative voting rights for the majority but wanted a similar right in favour of the nominee directors of the SP Group. The Supreme Court observed that the frequent change in their position raised a doubt whether it is actually a fight on principles. Supreme Court observed that the affirmative voting rights if bad in principle, surprisingly become good if conferred on SP Group.

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- The Articles of Association of Tata Sons continue to contain the prescribed restrictions which make it a private company within the definition of the expression under Section 2 (68). The provisions of Sections 149 (4), 151, 1771 (1) or 178 (1) of the said Act would not apply to Tata Sons.

- The principles of corporate governance, when scrutinized namely (i) that a large industrial house whose origin and creation was familial was willing to handover the mantle of heading the entire empire to a person like CPM and that (ii) that the identification of CPM as the successor to RNT was done by the very same nominees of the two Tata Trusts, make it clear that the Tata Group was guided by the principle of corporate governance (even without a statutory compulsion) and not by tight fisted control of the management of the affairs of the Group.

- Affirmative voting rights for the nominees of institutions which hold majority of shares in companies have always been accepted as a global norm and the rights conferred by Article 121 conferred only a limited right upon the Directors appointed by the Trusts, namely about the manner in which matters before any meeting of the Board shall be decided.

- Objections were raised about RNT vetting the minutes of meetings of the Board and his participation as a shadow Director. However, it was noted by the Supreme Court that CPM himself sought guidance of RNT while accepting the office of Executive Chairman. CPM also recorded his desire to RNT's continued support and guidance.

- Thus, the challenge to the affirmative voting rights and the allegations revolving around pre consultation by the trusts of all items in agendas and RNT's indirect or direct influence over the board were all rejected by the Supreme Court.

4b. Claim for proportionate representation

- The right to claim proportionate representation is not available to a minority shareholder statutorily, both under the 1956 Companies Act and under the 2013 Companies Act. Under Section 252 (1) of the 1956 Act and Section 151 of the 2013 Act, the spotlight was only on "small shareholders" and not on "minority shareholders".

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Such right is hence only available to a small shareholder, which SP Group does not qualify (holding 18.37% shareholding valued at around Rs. 58,441 crores and having received aggregate dividends to the tune of Rs. 872 crores).

- It is noted that such a right is not available even under the Articles of Association of the Company, i.e. contractually. Neither the SP Group nor CPM could request the NCLT to rewrite the contract, by seeking an amendment of the Articles of Association. These Articles as they exist, are binding upon SP Group and CPM by virtue of Section 10(1) of the said Act.

- Realizing that the complainant companies do not have such right, they claimed for the existence of a quasi-partnership between the Tata Group and SP Group. It was contended that there existed a personal relationship between the management of SP Group and those in management of Tata Sons for over several decades.

- The Supreme Court held that the SP Group became a shareholder after 50 years and CPM's father was inducted into the Board, after 15 years of acquisition of shares and such induction was not in recognition of any statutory or contractual right. Hence there was nothing on record to show that there was either (i) a pre-existing relationship before the incorporation of the company or (ii) a living in relationship picked up halfway through, by entering into an agreement in the nature of a partnership. The argument of the existence of a personal relationship, leading to a right and legitimate expectation to have a representation on the Board, was rejected by the Supreme Court.

5. Conversion from Public to Private Company

- Tracing the history of the incorporation of Tata Sons and the changes in law relating to the provisions of "public company" and "private company", the Supreme Court held that falling back on Section 465 (3) of the 2013 Act, they came to a conclusion that Section 2 (68) of the 2013 Act, will prevail over Section 3 (1) (iii) of the 1956 Act. As an effect thereof, on and from 12th September, 2013, the question whether a company is a private company or not will be determined only by the definition of the expression "private company" found in Section 2 (68) of the 2013 Act.

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- The Supreme Court noted that the Articles of Association of Tata Sons contained the restrictions as prescribed in sub clauses (a) to (c) of Section 3 (1) (iii) of the 1956 Act, but not the requirement of sub clause (d) incorporated in the year 2000, however on and from 12th September, 2013 (date of coming into effect of Section 2 (68) of the 2013 Act), the Articles of Association of Tata Sons satisfied the requirements of Section 2 (68) of the 2013 Act. It therefore was and continued to be a "private company".

- As regards, the procedure adopted for change of status of the Tata Sons from a Public Limited Company to Private Limited Company, the Supreme Court held that there was no "illegality" in the same as the status of a company is determined by the Articles of Association and the statutory provisions and the certificate is a mere recognition of the status of the company, and it does not by itself create one.

- It was held that the request made by Tata Sons and the action taken by Registrar of Companies to amend the certificate of incorporation which included the words "Private" was perfectly in order. Reliance was placed on a decision of the Supreme Court in *Darius Rutton vs. Gharda Chemicals Ltd.*, where the court recognized the possibility of a deemed public company reverting back to its status as a private company by incorporating necessary provisions in the Articles.

Conclusion:

The result is that all questions of law were answered in favour of the Tata Group and all appeals filed by the Tata Group were allowed and the cross-appeals of SP Group stood dismissed. The original company petition and all applications were also dismissed by the Supreme Court.

An application made by the SP Group praying for alternate relief of directing Tata Sons and others to cause a separation of ownership interests of SP Group in Tata Sons through a scheme of reduction of capital by extinguishing the shares held by SP Group in lieu of fair compensation, was rejected by the Supreme Court.

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This was rejected on the ground that in an Appeal under Section 423 of the said Act, the Supreme Court is concerned with questions of law arising out of the order of the NCLAT and that this Court could not at this stage adjudicate on fair compensation (which needs adjudication on facts of various items) and left it to the parties to take the Article 75 route or any other legally available route in this regard.

Latest Developments:

It is now understood that the SP Group has recently filed a Review Petition in the Supreme Court for a review of this order. The same is now pending.