Law of Arbitration in relation to a proceeding under section 397/398 of Companies Act, 1956

A brief:

Alternative Dispute Resolution Mechanism (ADR) is encouraged in view of the fact that there exists an unreasonable delay in the Courts. Among the other modes of Alternative Dispute Resolution (ADR), dispute resolution through Arbitration in accordance with the provisions of Arbitration and Conciliation Act, 1996 is being encouraged now. I am of the opinion that the Arbitration Mechanism is better suited for resolving corporate disputes and where there exists a consensus on “Arbitrator” and the procedure to be followed. I strongly feel that the Arbitration Mechanism may not produce the intended results if the right to choose an Arbitrator or the Tribunal is conferred on only one party through the clause. Though it is strongly felt that the ADR is to be encouraged in view of the delay in courts etc., there are critics criticizing the Arbitration Mechanism and especially when it is forced on a party. Constitutional Courts have discussed the scope of many provisions under the Arbitration and Conciliation Act, 1996 from time to time and I am personally impressed with the observations made by the Apex Court in **SBP & Co. v. Patel Engg. Ltd (2005 (8) SCC 618)**. But, when it comes to understanding the ratio laid-down by the Constitutional Court in SBP & Co. v. Patel Engg. Ltd (2005 (8) SCC 618), in my opinion, there is no clarity. As per my understanding, the ratio laid-down by the Apex Court and followed subsequently on the scope of section 11 of Arbitration and Conciliation Act, 1996 is automatically applicable to an application under section 8 of the Arbitration and Conciliation Act, 1996. Many questions tend to arise still on various provisions of Arbitration and Conciliation Act, 1996 and we also require few more reforms in the law taking ground realities into consideration.

But, it is true that when the parties are agreed for referring their dispute to an ‘Arbitrator’ and the agreed on all connected issues, then, the Arbitration Mechanism is better suited for getting the disputes resolved. Despite all the encouragement to the ADR in view of the apparent failure of courts, the ADR through Arbitration is also being criticized and I believe that, very shortly, the focus will be on bringing further reforms on the law of Arbitration and especially Domestic Arbitration Mechanism in India. The ADR is to be seen from two angles ie., from the point of view of the industry and from the point of view of the common man. The issue of providing speedy and efficient dispute redressel mechanism is a larger issue to deal with and it will emerge as imperative soon forcing the governments to think at the ground realities and the required reforms. But, when we look at the dispute resolution for the purpose of industry or business people, it is true that ADR through Arbitration is better suited for the industry provided certain issues are addressed in the course.

Law of Arbitration and section 397/398 of Companies Act, 1956:

I am always of the view that certain issues can not be referred to Arbitration and the Arbitration mechanism can not fulfill the object of certain legislations effectively; the apparent example being the proceeding under section 397/398 of the Companies Act, 1956. All are aware at the complications in getting the corporate disputes resolved and the complications in a proceeding under section 397/398 of the Companies Act, 1956. It is also very frequently seen now in a

proceeding/petition under section 397/398 of the Companies Act, 1956, an application under section 8 of Arbitration and Conciliation Act, 1956 is being filed based on an Arbitration Clause asking for reference of the dispute to the Arbitration. I am not referring the judgment of the constitutional courts, but, I strongly feel that the application of law of Arbitration in a proceeding under section 397/398 of the Companies Act, 1956 will remain complicated. Already there is a perception among corporates that the remedy provided to the shareholders when they are oppressed or the company is mismanaged, is not effective. The issue of application of law of arbitration to a proceeding under section 397/398 of the Companies Act, 1956 further complicates the entire thing. First of all, I would like to say as to why law of Arbitration can not be imposed mechanically in a proceeding under section 397/398 of the Companies Act, 1956 and it is as follows:

1. Adjudication of a corporate dispute under section 397/398 of the Companies Act, 1956 requires expertise and that is also a reason for constituting "Company Law Board" or the "Tribunal" especially under the provisions of Companies Act, 1956.

2. A proceeding under section 397/398 of the Companies Act, 1956 can not be seen as a proceeding between or among the shareholders only and it is the responsibility of the Company Law Board to look into the functioning of the company, other shareholders, other stake holders, rights of other third parties who are not involved in the proceeding too apart from public interest. In view of the scope of a proceeding under section 397/398 of the Companies Act, 1956, an Arbitrator or an Arbitral Tribunal can not effectively deal with a case of oppression and mismanagement.

3. A proceeding under section 397/398 of the Companies Act, 1956 will normally be based on a series of acts on the part of the majority in the Company and as such no Arbitration clause can effectively cover the scope of allegations in a petition under section 397/398 of the Companies Act, 1956.

4. The object of the Company Law Board under section 397/398 of the Companies Act, 1956 is to 'put an end to the mattes complained of' and in order to 'regulate the affairs of the Company'. In view of the scope of section 397/398 and the object, Company Law Board may simultaneously look into a particular issue though that particular issue is a subject matter of a Civil Suit or some other proceeding. The object of section 397/398 of the Companies Act, 1956 is different from the scope of a Civil Suit or some other proceeding.

Thus, it is likely that the object of section 397/398 and other provisions of the Companies Act, 1956 may get defeated if law of Arbitration is made applicable automatically or mechanically. Without referring to any judgments on the issue, I strongly feel that the jurisdiction of the Company Law Board/Court/Tribunal under section 397/398 of the Companies Act, 1956 can not be taken-away unless the Company Law Board/Court/Tribunals feels that there is nothing wrong in referring the dispute to the Arbitration or the Tribunal based on the averments in the Petition and other considerations. It is also true that, at times, share-holders will do forum-shopping and may feel comfortable approaching the Company Law Board though a particular dispute can be

decided by a Civil Court. This is where the Company Law Board can seriously look into the issue of Arbitration or referring the dispute to Arbitration and infact, logically, the Company Law Board need not entertain an application under section 397/398 of the Companies Act, 1956 at all as nothing prevents the parties to initiate the Arbitral proceedings simultaneously or the option of initiating the Arbitration proceedings is always open to any party despite a petition under section 397/398 of the Companies Act, 1956 being dismissed. From any angle, I don't think that the jurisdiction of the Company Law Board under section 397/398 of the Companies Act, 1956 can be taken-way showing an Arbitration clause and if such a proposition is accepted, then, the object of section 397/398 of the Companies Act, 1956 will get defeated. Its another complicated issue and to be handled carefully despite the encouragement to the ADR through Arbitration.

[**Note:** the views expressed are author's personal point of view.]