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The Case for Mandatory Pre-Institution Mediation for Indian Shareholder Disputes

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While dust settles on the passing of the Mediation Act, 2023 ("**Mediation Act**"), many have already written about the different dimensions of mediation under it. India's mediation regime is unique for not only promoting indigenous modes of mediation, but also for championing mandatory statutory mediation. This includes the obligation to mandatorily utilise the pre-institution mediation ("**PIM**") processes under section 12A of the Commercial Courts Act, 2015 ("**CC Act**") or under section 18(2) of the Micro, Small and Medium Enterprises Development Act, 2006 ("**MSMED Act**"), where the plaintiff is obligated to institute mediation proceedings prior to the initiation of legal proceedings. While many continue to criticise this for rendering a voluntary process involuntary, it cannot be stressed enough that the success of even a few PIMs under the CC Act and MSMED Act considerably reduces the burden on the overstressed court machinery (see PIM data for Delhi courts here – in India, PIM is generally conducted by the relevant legal services authority of the district – for instance, for the Shahdara district in Delhi, PIM would be conducted by the Delhi State Legal Services Authority).

In spite of the above, shareholder disputes still remain neglected when it comes to mandatory PIM. While the Mediation Act does make changes (yet to come into force) to the Companies Act, 2013 ("**Companies Act**") to grant the National Company Law Tribunal ("**NCLT**", the adjudicatory body for statutory shareholder disputes in India) powers to compel parties to mediate, these changes do not include mandatory PIM.

The amended section 442(2) of the Companies Act states that "[*n*]*othing in this section shall prevent the Central Government, Tribunal or the Appellate Tribunal before which any proceeding is pending from referring any matter pertaining to such proceeding suo motu to mediation to be conducted under the provisions of the Mediation Act, 2023 as the Central Government, Tribunal or the Appellate Tribunal, deems fit*". It appears that the aforesaid addition is in line with the view that mandatory mediation can succeed even if the parties' consent to mediation does not exist initially.

In November 2023, the England and Wales Court of Appeal in *Churchill v Merthyr Tydfil County Borough Council*, [2023] WLR(D) 498 held that "*even with initially unwilling parties, mediation can often be successful*". The benefits of mandatory mediation have also been highlighted by the Supreme Court of India ("**SCI**") in *Patil Automation Pvt Ltd and Ors v Rakheja Engineers Pvt Ltd*, (2022) 10 SCC 1 where the SCI opined that "*the realisation has been growing over a period of time, that formal court rooms, long drawn-out proceedings, procedural wrangles, mounting and crippling costs, delay, which never wanes but only increases with the day that at least, in certain*

categories of cases, mediation can be the way out" – all these flaws listed by the SCI are also similarly applicable to the manner in which shareholder disputes are adjudicated.

Nowadays, there is an increasing trend in India towards the incorporation of arbitration clauses in shareholder agreements. While this is generally restricted to companies who have access to sophisticated legal advice, and while the enforceability of such arbitration clauses for all shareholder issues still remains unclear (see here), Indian courts have opined that even the existence of arbitration clauses would not preclude the exercise of jurisdiction by the NCLT. In *Rakesh Malhotra v Rajinder Kumar Malhotra and Others*, (2014) SCC OnLine Bom 1146, the High Court of Bombay stated that the powers of the NCLT in respect of the oppression remedy "*are not powers that can be exercised by a civil court. They certainly cannot be exercised by an arbitral forum*". In view of this, shareholders alleging oppression would still retain their hypothetical right to institute PIM proceedings even if an arbitration clause between the said shareholders exists. For the reasons outlined below, shareholder disputes may well represent the greatest opportunity for mandatory pre-institution mediations to succeed in India.

First, shareholder disputes in India often arise out of situations where trust between different shareholders has broken down irretrievably. This is because contrary to the position in many other jurisdictions, the oppression and mismanagement remedy in India requires that for minority shareholders to claim reliefs, they have to demonstrate that the circumstances also justify a just and equitable winding up of the company (please see section 242(1)(b) of the Companies Act).

As the Privy Council stated in *Chu v Lau*, [2020] UKPC 24 (quoted with approval by the SCI in *Tata Consultancy Services Limited v Cyrus Investments Private Limited and Others*, (2021) 9 SCC 449), "*just and equitable winding up may be ordered where the Company's members have fallen out in two related but distinct situations*". These two situations are one of "*functional deadlock*" where there is "*an inability of the company to function at board or shareholder level*", and "*where the company is a corporate quasi-partnership, an irretrievable breakdown in trust and confidence between the participating members may justify a just and equitable winding-up, essentially on the same grounds as would justify the dissolution of a true partnership*".

Classic cases of shareholder oppression in India often relate to situations where there has been an irretrievable breakdown of trust between people effectively acting as partners or where a deadlock exists. Mediation, as opposed to adversarial proceedings before the NCLT, is better suited to repair relationships, rebuild trust and resolve deadlocks.

Second, it is reported that around 85% of all Indian companies are closely-held, family-owned companies. While this attribute of Indian companies is not unique, what is unique to the Indian sociological context is the fact that a large number of these companies are incorporated in the context of Indian joint families (and the very unique concept of a Hindu Undivided Family).

Essentially, Indians have historically sought to accumulate capital as a family, and the incorporation of closely-held companies is a modern take on capital accumulation as a family unit. Needless to say, these commercial arrangements have always been based on a relationship of mutual trust and confidence between different family members. When these relationships waver and trust breaks down, mediation may be more beneficial than adversarial processes in repairing relationships and ensuring the continuity of both, the business and the family unit. Unlike disputes under the CC Act or the MSMED Act, the parties to a shareholder dispute are ordinarily persons who were already participating together as shareholders in the same company and probably had

close relationships with each other at one point of time (or their forbearers did).

Finally, as a matter of practice, Indian courts, by virtue of their heavy workload, are not the best equipped to expeditiously hear cases of shareholder oppression. As has been stated above, in India, such cases are generally heard by regional benches of the NCLT who are also empowered to decide cases under the Insolvency and Bankruptcy Code, 2016 ("**IBC**"). More days are allocated by NCLTs for cases under the IBC as compared to cases arising under the Companies Act. For instance, the NCLT bench in New Delhi hears Companies Act cases one day of the week and reserves the other four days for IBC cases. On account of their heavy workload, this bench also routinely hears around 40-50 cases daily. Clearly, the statutory machinery for the adjudication of shareholder disputes in India appears to be overburdened and any reduction of cases from its roster should be of benefit. In view of considerations of expediency, mandatory PIM could go a long way in reducing the burden on NCLTs.

In conclusion, it is often remarked in Indian legal corridors that a large portion of shareholder disputes in India actually arise on account of a clash of egos. In such charged-up situations where trust has broken down between individuals who otherwise may have had a history of successfully working with each other, mediation presents an avenue to do immeasurable good by repairing such relationships before shareholder oppression proceedings are instituted.

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