IN THE HIGH COURT OF JUDICATURE AT BOMBAY
CIVIL APPELLATE JURISDICTION

WRIT PETITION NO.3196 OF 2017
WITH
CIVIL APPLICATION NO.623 OF 2017

Ramesh Shantilal Modi & anr. ... Petitioner

Vs.

Modi Landscape Pvt. Ltd. & Ors. … Respondents

with
WRIT PETITION NO.3194 OF 2017
with
CIVIL APPLICATION NO.621 OF 2017

Ramesh Shantilal Modi & anr. ... Petitioner

Vs.

Modi Landscape Pvt. Ltd. & Ors. … Respondents

with
WRIT PETITION NO.3195 OF 2017
with
CIVIL APPLICATION NO.622 OF 2017

Ramesh Shantilal Modi & anr. ... Petitioner

Vs.

Modi Landscape Pvt. Ltd. & Ors. … Respondents

Mr.A.Y. Sakhare, Sr.Advocate with Joel J. Carlos and Amarnath Vibhute i/b R.S. Mirpury for Petitioners & for Applicants in CAs

Mr.Vivek Kantawala with Ms.Bhairavi Waravdekar, Mr.Amey Patil i/b M/s.Vivek Kantawala & Co. for Respondent Nos.1,2 & 3

Mr.P.S. Dani, Senior Advocate i/b S.C. Wakankar for Resp. Nos.4 to 8

CORAM: Mrs.MRIDULA BHATKAR, J.
DATED: APRIL 27, 2017

P.C. :

1. In these petitions filed under Article 227 of the Constitution of India, the impugned order dated 9.2.2017 of the learned District Judge 10, Pune, sending the matter to the Arbitrator from the Civil Court thereby setting aside the order dated 28.11.2016 below exhibit 40 in RCS No.1851 of 2016 passed by the learned 7th Joint Civil Judge, Junior Division, Pune is challenged. The petitioners are the plaintiffs who filed a suit bearing no. /2016 against the defendant No.1 – a private limited company having a business of land dealings and development, of which they are all the Directors. Defendant Nos.2, 3 and 4 are the other two Directors of the defendant No.1 – company. Defendant No.5 is a registered partnership firm, wherein Defendant Nos.4, 6 to 8 are the partners. Thus, the defendant No.4 is facing prosecution by the plaintiffs in a dual capacity as a Director of the defendant No.1 – company and a partner of the partnership of defendant No.5 – Firm. Defendant

No.1 – company is a company in the business of land dealings, development of the land and construction of tenaments. The plaintiffs hold 40% shares of the company. Defendant Nos.2 and 3 joined the company in 2016 as Directors of the company and they jointly hold 35% of the shares. Defendant No.4 also jointed the company in the year 2012 and acquired 25% shares of the company. On 16.8.2013, defendant No.1 – company entered into two joint venture agreements with defendant No.5 – Firm in respect of the business. To open a joint escrow account in the name of defendant No.1 – company and defendant No.5 – Firm is one of the major terms and condition of Joint Venture Agreement. The money will be deposited in the said escrow account proportionate to the shares of the company and the partnership firm and the funds will be transferred proportionately to the shares of defendant No.1 – company and defendant No.5 – Firm. Inter alia, the business activities were jointly conducted, however, the monies earned by way of income or profit were paid to defendant No.5 - Firm partnership firm only. No escrow account was opened as agreed between the parties and as per the case of the plaintiffs, the entire money which was earned out of the business conducted pursuance to the joint venture agreements, were siphoned off in the account of partnership firm alone. Thus, being aggrieved by such fradulent activities, the plaintiffs were constrained to file civil suit for mandatory and directory injunction against the Defendants. During the pendency of the suit, the Defendants separately filed three applications i.e., exhibits 35, 37 and 40 with a prayer that in the joint venture agreements dated 16.8.2013, the parties have agreed to incorporate an arbitration clause and, therefore, the parties are to be referred to the arbitrator and the jurisdiction of the civil Court is ousted.

2. The trial Court rejected the applications and held that the plaintiffs have pleaded fraud and while relying on the judgment of the Supreme Court in **A. Ayyasamy vs. A.Paramasivam & ors.**[1] has held that a suit based on fraud cannot be referred to the arbitrator and hence, held that the trial Court has jurisdiction to try and entertain the suit. The said order dated 18.11.2016 was challenged in appeal in Miscellaneous Appeal No.499 of 2016 by the defendants and the learned District Judge, Pune set aside the order and by order dated 9.2.2017 allowed the appeal and referred the dispute between the plaintiffs and the defendants to arbitration. Hence, this petition.

1 (2016) 10 SCC 386

3. Mr.Sakhare, the learned Senior Counsel appearing for the petitioners, submitted that the order passed by the learned District Judge is not consistent with law and requires to set aside. He dealt with the pleadings and averments made in the plaint. He argued that the plaintiffs are holding 40% of the shares and Defendant Nos.2 and 3 are holding 35% shares and the remaining 25% shares are held by defendant No.4. Thus, the defendant Nos.2, 3 and 4 are the majority shareholders holding 60% of the total shares and the plaintiffs are in minority. The defendant No.4 is working in a dual capacity as a Director and also as a partner in the defendant No.5 – Firm, though he was not authorized and no such resolution was passed by the Board of Directors of the company, he has signed in the capacity of the Director to transfer the monies. The business of the company was completely taken over by the partnership firm and though the income and whatever profits were earned out of this business was completely enjoyed by the Defendant No.5 firm and its partners i.e., defendant Nos.4, 6, 7 and 8. The escrow account was not opened and no money was deposited in the said account. He submitted that the plaintiffs have given the details of the nature of the fraud committed against the

Defendant Company by other defendants. It was argued that the Defendant company itself cannot take action against the wrong-doers. The majority of the shares are with the defendants who are the wrong-doers and thus, naturally, no action is initiated by the Defendant – Company against the partnership firm where defendant No.4 is one of the partners. He submitted that the suit is based on a derivative action and so, it cannot be sent to arbitration. In support of his submissions, he relied on the judgment of a learned Single Judge of this Court in the case of **Onyx Musicabsolute.com Pvt. Ltd. & Ors. vs. Yash Raj Films Pvt. Ltd. & Ors.**[2]

4. The learned Counsel has further submitted that in the judgment of the learned District Court, the learned District Judge has given a complete go-by to this point. He has further submitted that in fact, there was no agreement as such between the parties i.e., plaintiffs and the Defendants and therefore, this matter cannot be before the arbitral tribunal. He relied on the joint venture agreements and submitted that though the plaintiffs have signed the said agreements, they have specifically signed in a capacity of Directors of the said defendant No.1 – company and have not

2 2008 (6) Bom.C.r. 418

signed in the personal capacity as shareholders. The plaintiffs have filed the suit in their personal capacity as minority shareholders in order to protect the financial and administrative interest of the defendant No.1 – company which is not to be mixed up by taking them as signatory to the joint venture agreements.

5. He further submitted that the learned District Judge has erred in stating that the plaintiffs have condoned the action of misappropriation and the plaintiffs have forgone the criminal action against the Defendants. The learned Senior Counsel argued that throughout the plaint, when there are specific averments in respect of fraud and misappropriation of money, the learned District Judge ought not to have given such reasoning while allowing the application of the defendants and sending the matter to the arbitral tribunal.

6. Mr.Dani, the learned Senior Counsel for respondent Nos.4 to 8, submitted that this petition is in fact not maintainable in view of section 37 of the Arbitration and Conciliation Act. He submitted that the order refusing to refer the parties to arbitration passed by the learned trial Judge is challenged in appeal filed under section 37(1) of the Act by the present respondents and it was allowed by

the learned District Judge. As per section 37(3), no second appeal lies from the order passed in appeal under the said section. However, the section has kept alive his right to appeal in the Supreme Court.

7. The learned Senior Counsel further argued that in view of appeal provisions made under section 37, the Legislature has narrowed down the scope of appealable orders and has restricted to only first appeal and the second appeal cannot be filed in a routine course but if it wants to challenge, then only before the Supreme Court. He submitted that the order passed by the learned District Judge is justified in view of section 8 of the Arbitration and Conciliation Act as is amended in 2015. He submitted that by way of amendment, the Legislature has expanded the scope of section 8 and even persons who are not parties to the agreement also can be involved in the arbitration proceedings. To take out from the scope of section 8, the only specie required is non-existence of the valid agreement, then only the matter cannot be referred to arbitrator. In the present case, there is an agreement between the parties with arbitration clause No.32 and thus, the District Judge has rightly set aside the order

passed by the trial Court.

8. The learned Senior Counsel in support of his submissions in respect of section 8 and fraud, has further submitted that section 8 and the subject matter before the arbitration, especially the cases involving fraud, also relied on judgment of the Supreme Court in **A.Ayyasamy (supra).** He pointed out that the Supreme Court has in the said judgment, on the point of jurisdiction, has relied on the ratio laid down in **Sundaram Finance Ltd. vs. T.Thankam**[3]. He further submitted that though the cases of fraud are not to be referred earlier to the arbitrator, the Supreme Court on the judgment of **A.Ayyasamy (supra)**, has considered the aspect of fraud and has held that if fraud is of voluminous nature affecting the public domain, such matter cannot be referred to arbitrator. However, in the present case, the plaintiffs have claimed misappropriation in respect of profits and income of the company and the partnership firm and hence, the dispute was likely referred to the arbitrator. He further submitted that while meeting the issue of derivative action, he relied on the judgment of a learned Single Judge of this Court in the case of **Rashmi Mehra & Ors. vs. The EAC Trading Ltd. & Ors.** in Notice of Motion No.1092 of 2006 in

3 AIR 2015 SC 1303

Suit No.961 of 2006 dated 8.11.2006. He submitted that this judgment of the learned Single Judge in the said matter is earlier to the judgment of **Onyx Musicabsolute.com Pvt. Ltd. & Ors. (supra),** and the learned judge has taken a view that even if the suit is based on derivative action, the proceedings can be taken to the arbitral Tribunal.

9. Mr.Kantawala, appearing for respondent Nos.1, 2 and 3 adopted the submissions of Mr.Dani and further added that the plaintiffs have taken out the proceedings before the National Company Law Tribunal, Mumbai (NCLT). The derivative action has thus been diluted. It is submitted that the plaintiffs have suppressed this fact from this Court and there is no whisper about the said proceedings in this petition.

10. Mr.Kantawala further relied on the judgment of the Supreme Court in the case of **Chloro Controls (I) P. Ltd. vs. Severn Trent Water Purification Inc. & Ors.**[4] to submit that the Supreme Court has held that even a third person claiming through or under a signatory party, can be subjected to arbitration proceedings as the Supreme Court has held that the expression “person claiming

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4 2013 (1) SCC 641

through or under" would mean and take within its ambit multiple and multi-party agreements, though in exceptional cases and even the non-signatory parties to some of the agreements can be provided and be referred to arbitration provided they specify the 3 requisites under sections 44 and 45 r/w schedule I. Reference to non-signatory parties is neither unknown to arbitration jurisprudence nor is it impermissible.

11. Mr.Sakhare, in reply, submitted that the judgment relied by Mr.Kantawala, is not applicable as sections 44 and 45, under Chapter II are concerned with international covenants and awards. He reiterated that the plaintiffs' case is based on fraud and the details are given in the pleadings, it is to be covered under the directions given by the Supreme Court in the case of **A.Ayyasami (supra)** which are the non-arbitrable disputes.

12. He further submitted that the judgment of the learned Single Judge of this Court in **Rashmi Mehra & Ors. (supra)** also cannot be relied because this judgment is also given when the Notice of Motion u/s 45 of the Arbitration and Conciliation Act was taken out and it was also pertaining to agreement of foreign collaboration and thus, these are different provisions. He further submitted that

the points raised here on behalf of the respondents are totally different. The reasons given by the learned District Judge mainly a allowed the application on the ground that there is condonation of misappropriation and fraud.

13. It is useful to reproduce relevant portion of Section 8 of the Arbitration & Conciliation Act which reads thus:

> "8. Power to refer parties to arbitration where there is an arbitration agreement. (1) A judicial authority, before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party to the arbitration agreement or any person claiming through or under him, so applies not later than the date of submitting his first statement on the substance of the dispute, then, notwithstanding any judgment, decree or order of the supreme court or any Court, refer the parties to arbitration unless it finds that prima facie no valid arbitration agreement exists.
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> …."

14. If there is an agreement between two parties, wherein arbitration clause is included, then, that matter is to be referred to the arbitrator and the scope of section 8, thus, covers not only the parties to the agreement but also the other third parties who are claiming through or through whom the parties to the agreement claim. In the present case, both the petitioners have signed the agreements having arbitration clause.

15. The petitioners/original plaintiffs have pleaded fraud and have not condoned the criminal action. The submissions of the learned Counsel Mr.Sakhare that the learned District Judge has erred in holding that the plaintiffs have condoned the delay in the criminal action, is correct. If the petitioners want to lodge a criminal action against them, then, they are free to take the same which is another issue. However, the fraud pleaded is of the nature of misappropriation of the accounts and of signing the documents including the cheques without having any authority through proper resolution of the board of directors of the Respondent No.1 company. Thus, it appears that the petitioners have the main grievance against the working of and financial mismanagement done by respondent No.4. Thus, it transpires from the pleadings that there is a fraud. However, this fraud is not of such serious nature, which is so complicated that it cannot be dealt with by the arbitrator. The cases of dispute pertaining to accounts, financial management in the company or partnership firm are not non-arbitral disputes. The arbitral Tribunal can very well deal with such type of disputes. When any Corporation, company or partnership firm enter into a business agreement and

there is a possibility of some differences and disputes and in order to meet such possible disputes, an arbitration clause is incorporated in such agreement. Thus, the financial dispute is one of such anticipated disputes which can be taken before the arbitral Tribunal. Fraud which is of very complex nature having a pervasive effect on public and which may require very lengthy and complex evidence, cannot be taken before the arbitral Tribunal and the civil Court is the only forum to deal with such litigation. However, considering the pleadings in the present case and the nature of a dispute and as there is inclusion of arbitration clause No.32 in the joint venture agreement, I am of the view that the matter, the decision of the District Judge to refer the dispute to the Tribunal cannot be faulted with.

16. I place complete reliance on the ratio laid down in **A.Ayyasami (supra),** as it is the latest judgment of the Supreme Court. Though fraud is considered as non-arbitrable dispute in the said judgment, it is explained by the Division Bench of the Supreme Court in the light of amended section 8 of the Act that mere allegations of fraud in the pleadings by one party against the other cannot be a ground to hold that the matter is incapable of

settlement in arbitration and should be decided by the civil Court. It is further said that the allegations of fraud should be such that not only these allegations are serious that in normal course, these may even constitute criminal offence. They are also complex in nature and the decision on these issues demands extensive evidence for which the civil Court should appear to be more appropriate forum than the arbitral Tribunal. In the case of **A.Ayyasami (supra)**, the Supreme Court has considered the earlier judgment in **Abdul Kadir Shamsuddin Bubere vs. Madhav Prabhakar Oak**[5] (supra) wherein it was held that where a case relates to fraud and serious mal-practices, then, the detailed evidence is required that cannot be properly gone into by the arbitrator. It also considered the case of **N. Radhakrishnan vs. M/s.Mastero Engineers**[6], wherein the said view was reiterated by the Supreme Court. However, the Division Bench of the Supreme Court has while dealing with the amended section 8 by which the scope of arbitration is enhanced, has held that section 8 of the new amended act, embodies a conscious departure which is intended to strengthen the efficacy of arbitration.

5 AIR 1962 SC 406
6 (2010) 1 SCC 72

17. The submissions of Mr.Sakhare that there are allegations of fraud, are not mere allegations but the petitioners/plaintiffs have given the details of the fraud and the accounts. Considering the ratio laid down in the case of **A.Ayyasami & Ors (supra),** though there is a dispute involving fraud as it is not of complex nature, it can be referred to the arbitral Tribunal. The court has held thus:

> "37. …. In each such case where an objection on the ground of fraud and criminal wrongdoing is raised, it is for the judicial authority to carefully sift through the materials for the purpose of determining whether the defence is merely a pretext to avoid arbitration. It is only where there is a serious issue of fraud involving criminal wrongdoing that the exception to arbitrability carved out in N. Radhakrishnan may come into existence. Allegations of fraud are not alien to ordinary civil courts. Generations of judges have dealt with such allegations in the context of civil and commercial disputes. If an allegation of fraud can be adjudicated upon in the course of a trial before an ordinary civil court, there is no reason or justification to exclude such disputes from the ambit and purview of a claim in arbitration. Parties who enter into commercial dealings and agree to a resolution of disputes by an arbitral forum exercise an option and express a choice of a preferred mode for the resolution of their disputes. Parties in choosing arbitration place priority upon the speed, flexibility and expertise inherent in arbitral adjudication. Once parties have agreed to refer disputes to arbitration, the court must plainly discourage and discountenance litigative strategies designed to avoid recourse to arbitration. Any other approach would seriously place in uncertainty the institutional efficacy of arbitration. Such a consequence must be eschewed."

18. In respect of derivative action, it is useful to refer to the two

cases which are relied on the by the learned Counsel for the petitioners and the respondents. It is an admitted fact that the suit is based on derivative action as the plaintiffs are minority shareholders and respondent No.1 is a company and respondent Nos.2 to 4 are the majority shareholders. The main grievance is pleaded against respondent No.4 being a partner of the Respondent No.5 partnership firm. He has siphoned the company's money to the accounts to the firm instead of putting it in the escrow account. In fact, the escrow account, as agreed to between the parties, was not opened. Thus, from the averments, a case of fraud or falsification of the accounts or misappropriation of the funds is alleged against the respondent No.4 and other respondents who are also partners of the firm.

19. In the case of Onyx **Musicabsolute.com Pvt. Ltd. & Ors. (supra)**, a notice of Motion so also an arbitration petition were preferred praying that the issue was more or less the same, where there was an agreement consisting of arbitration clause and the plaintiffs were minority shareholders in the company and it can be culled out from the said judgement that if the company is defrauded by insiders to control it by the director or the person,

who held a majority shares, then, the company cannot take any action to protect its own property and a derivative action by such shareholder for wrong to a company is maintainable. Under such circumstances, therefore, the said suit is maintainable and the learned Judge further held that the derivative action by way of arbitration cannot be taken by initiating arbitration before arbitral Tribunal. He further held that such action is legal action before the public forum i.e., ordinary course of law and not before a private forum of arbitral Tribunal. The arbitral Tribunal gets jurisdiction only on agreement between the parties. In the case of **Onyx Musicabsolute.com Pvt. Ltd. & Ors. (supra),** there was an agreement between the plaintiff No.1 and defendant No.1 and the other plaintiff Nos.2 to 5 were not the parties to the agreement.

20. In the case of **Rashmi Mehra & Ors. (supra)**, a learned Single Judge of this Court dealt with maintainabiity of a derivative action in arbitration. The learned Judge held thus:

> "37. While deciding the question of the maintainability of a derivate action in arbitration it is essential to note some of the essential features of a derivate action. Though a derivative action is filed in the name of the shareholder it is for the benefit of the company. The company is joined as a co-defendant. Most important, the reliefs if obtained enure to the benefit/credit of the

> company and not of the person bringing the derivative action. When bringing a derivative action to assert the rights of a company under a contract the person bringing the action is entitled to rely upon and enforce the contract in the same manner and to the same extent that the company itself could have. This is an obvious corollary to the aforesaid features of a derivative action.
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> 38. There is nothing to my mind that suggests that the arbitration agreement contained in such an agreement, stands on a different footing. The person who brings the derivative action invokes the arbitral clause not for himself but for and on behalf of the company. The action though not in form by the company is for all intents and purposes an action by and for and on behalf of the company. The person bringing the derivate action is therefore equally not only entitled to invoke but bound by, the arbitration clause qua the action. Obviously this will not be so qua the personal reliefs claimed. Thus seen there is no reason why a derivative action cannot be brought in arbitration proceedings."

21. Moreover, it is pointed out by the learned Senior Counsel Mr.Dani and Mr.Kantawala that the plaintiffs have filed the proceedings before the National Company Law Tribunal. Thus, it may dilute the derivative action.

22. In light of the above and in view of the expanded scope of section 8 of the Arbitration and Conciliation Act, I hereby dismiss the petition.

23. Mr.Sakhre, seeks a stay of this order for a period of six

weeks. Stay accordingly granted for a period of six weeks from today.

(MRIDULA BHATKAR, J.)