

IN THE HIGH COURT OF DELHI AT NEW DELHI

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Judgment delivered on: 22.07.2019

+ **ARB.P. 737/2017**

SHASHANK BHAGAT & ANR.

..... Petitioners

versus

SHEFALI VARMA & ORS.

..... Respondents

Advocates who appeared in this case:

For the Petitioners	: Ms Shyel Trehan and Ms Varnika Chawla, : Advocates.
For the Respondents	: Ms Namitha Mathews and Mr Pulkit : Malhotra, Advocates for R-1. : Mr Ashok Chhabra and Mr Nikhil Karwal, : Advocates for R-2 to R-12.

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HON'BLE MR JUSTICE VIBHU BAKHRU

JUDGMENT

VIBHU BAKHRU, J

1. The petitioners have filed the present petition under Section 11 of the Arbitration and Conciliation Act, 1996 (hereafter 'the A&C Act'), *inter alia*, praying that an arbitrator be appointed to adjudicate the disputes that have arisen between the parties in connection with the Agreement to Develop dated 29.10.2012 (hereafter referred to as 'the Agreement'). The Agreement was executed by respondent no.1 (Ms Shefali Varma) in her individual capacity claiming to be the legal

beneficiary of the estate of her father, late Sh Ashok Varma. She had also signed the Agreement on behalf of respondent nos. 2 to 12 (hereafter referred to as 'the Companies') as their Director. The recitals of the Agreement record that the Companies, acting through Ms Shefali Varma as a Director, had entered into an agreement dated 24.02.2011 with petitioner no.1 (Shashank Bhagat) for undertaking a group housing project under joint development on a plot of land, measuring 11.26 acres approximately, located in Sector-56 Gurgaon. The said agreement was referred to as 'Agreement with SV' in the Agreement (it is hereafter referred to as 'the 2011 Agreement'). Pursuant to the 2011 Agreement, petitioner no.1 had made a payment of ₹5,00,00,000/- (Rupees Five Crores) to Ms Shefali Varma which she had admitted having received for and on behalf of the Companies. In terms of the 2011 Agreement, petitioner no.1 had agreed to pay a consideration of ₹50 crores to the Companies for developing a housing project at his own expense. In turn, petitioner no.1 was entitled to 60% of the total built up area as well as proportionate common areas and the remaining 40% area would fall to the share of the Companies. It was also recorded that petitioner no.1 was entitled to enter into a tie-up with another developer and had, in fact, done so by entering into an agreement dated 02.03.2011 with M/s Eldeco Infrastructure and Properties Pvt. Ltd. for developing a housing project on the aforesaid land (land measuring 11.26 acres approximately, located in Sector-56, Gurgaon).

2. The Agreement also recorded that further addenda (four in number) to the 2011 Agreement had been entered and description of which was noted.

3. In terms of the Agreement, petitioner no.2 (Silverglades Holdings Private Limited) was appointed as the principal developer along with petitioner no.1 as a co-developer for developing the project on a minimum area of 10 acres, located within Ardee City in Sector-52, Gurgaon. The said land included a parcel of land measuring 5.78 acres being a part of the Group Housing Scheme known as 'Residency'. In consideration of the development rights, it was agreed that petitioner no.2 shall pay an aggregate consideration of ₹50 crores to the Companies. It was also acknowledged that Ms Shefali Varma had received an aggregate sum of ₹9 crores on behalf of the Companies, as detailed in the Agreement and the balance amount of ₹41 crores was agreed to be paid to the Companies in proportion of their land holding and in a manner as stipulated therein.

4. The petitioners claim that the disputes have arisen in connection with the Agreement and the same are required to be resolved by arbitration in terms of Clause 16 of the Agreement. The said clause is set out below:

“16. Arbitration

16.1 The Parties herein agree that any dispute or difference arising between the Parties under the Agreement shall be resolved amicably in the first instance. In case the Parties fail to arrive at a amicable settlement within 30 days of reference

thereof for amicable discussions, such unresolved disputes or differences shall be settled by arbitration referred to a sole arbitrator, to be mutually appointed by the disputing Parties in accordance with the provisions of the Arbitration and Conciliation Act, 1996 and any statutory amendments thereto from time to time.

16.2 The award of the Arbitrator/s shall be final and binding on the Parties to the Agreement. Neither Party shall be entitled to commence or maintain any action in court of law upon any matter in dispute arising from or in relation to this Agreement, except for the enforcement of an arbitral award granted pursuant to this Agreement. The place of Arbitration shall be Delhi. The arbitration proceeding shall be conducted in English language.”

5. The Companies dispute that they have entered into the Agreement as claimed by the petitioners. It is asserted on behalf of the Companies that Ms Shefali Varma had no authority whatsoever to enter into any agreement or accept any funds on their behalf. It is further alleged that Ms Shefali Varma had colluded with the petitioners and the Agreement is a nullity and cannot bind the Companies. It is further contended that even though the petitioners had purportedly entered into the Agreement with the Companies, the entire consideration had been paid to Ms Shefali Varma in her personal name.

6. Ms Shefali Varma also disputes that the Agreement is binding. She claims that the Agreement and the 2011 Agreement were contingent agreements and the same were conditional upon her and her

family members entering into a family settlement. She claims that since her family members could not arrive at any settlement, the Agreement ceased to be operative.

7. Ms Shyel Trehan, learned counsel appearing for the petitioners contended that Ms Shefali Varma was admittedly a director of the Companies at the material time and was, thus, empowered to act on their behalf. She submitted that Ms Shefali Varma was also accustomed to act on behalf of the Companies and in the circumstances, there was no occasion for the petitioners to make further enquiries as to whether she was duly authorized to enter into the agreements in question (the Agreement and the 2011 Agreement). She stated that the petitioners had conducted a due diligence exercise at the office of the Companies with the assistance of their employees and this was within the knowledge of the other family members of Ms Shefali Verma. She stated that in the circumstances, there was no occasion for the petitioners to doubt that Ms Shefali Varma was not authorized to act on behalf of the Companies. She contended that the doctrine of indoor management was squarely applicable in the facts of this case and the Companies could not be heard to state that they were not bound by the Agreement or the arbitration clause contained therein.

8. Mr Ashok Chhabra, learned counsel appearing for the Companies countered the aforesaid submissions.

9. The controversy involved in the present petition is limited to examining whether an arbitration agreement exists between the petitioners and the Companies. At the outset, it is relevant to refer to the 2011 Agreement (Agreement dated 24.02.2011, which is referred to as the Agreement with Ms Shefali Varma in the Agreement). Clause 2 of the recitals of the 2011 Agreement is relevant and is set out below:-

“SV has also represented that by virtue of being a Director/Authorised Signatory in the Land Owning Companies and in the Confirming Parties she will ensure and undertakes that she will be duly empowered and entrusted to sign and execute this Agreement for and on behalf of the above mentioned Companies.”

10. It is apparent from the above that although Ms Shefali Varma (SV) had signed the 2011 Agreement on behalf of the Companies, she had also represented and assured the petitioners that she would be empowered to sign and execute the said agreement. The future tense clearly implies that at the material time, the Companies had not passed any resolutions to authorize Ms Shefali Varma to sign the Agreement on their behalf.

11. Thereafter, on 19.12.2011, Ms Shefali Varma entered into an agreement – referred to as “Addendum to Agreement” – to amend the 2011 Agreement. The recitals of the said agreement (addenda) recorded that the father of Ms Shefali Varma (late Mr Ashok Varma) had executed a registered will dated 03.03.2005, bequeathing certain

properties and assets including certain land parcels and properties in Ardee City, Gurgaon to Ms Shefali Varma and her sister Ms Shibani Varma Kapur. It also recorded in Ms Shefali Varma's representation that a family settlement would be executed between the family members of late Sh Ashok Varma "*which will entitle her to the ownership and possessory rights of land measuring 11.26 Acres, situated at Village Wazirabad, Sector-57, Gurgaon, Harayna*". Ms Shefali Varma also represented that she would ensure that she will be duly empowered and entrusted to sign and execute the agreement for and on behalf of the aforementioned Companies.

12. A plain reading of the recitals of the "Addendum to Agreement" dated 19.12.2011 also indicates that the petitioners were duly aware that there were certain differences *inter se* the family members of Ms Shefali Varma and the Definitive Agreements could not be executed, since the disputes between the family members of Ms Shefali Varma had not been resolved. Clause 6 and 10 of the recitals of the said addendum are relevant and are set out below:-

"6. In terms of the aforesaid agreement, the Definitive agreement was to be executed by 31st March 2011, in anticipation that the issues relating to inter-se Family Settlement of SV would be resolved. However due to delay in the family settlement, SV and SB orally agreed to extend the time limit for execution of definitive agreement.

10. SV assured and represented that upon execution of a inter-se family settlement, a Definitive Collaboration Agreement shall be

executed between SV, SB and any nominated entity of the Silverglades Group.”

13. It is also relevant to refer to the recital F of the Agreement, which is set out below:-

“F. SV and the Owners have jointly represented that:-

- (i) The Owners being corporate entities are controlled and managed by the Varma Group comprising of Ashok Varma (AV) (since deceased), his wife Minakshi Varma (MV) two daughters namely Shefali Varma (SV) and Shibani Varma Kapur (SVK) being legal heirs of Sh. Ashok Varma.
- (ii) Ashok Varma expired on 1st June 2008 leaving his last and final registered Will dated 3rd March, 2005 duly registered vide Registration No.730 in Book No.3, Vol. No.471 on pages 149 to 153 on 24.06.2005 (copy annexed as **Annexure - E**) in accordance with which the equity shares of various companies of the group including the companies owning the said Land having interest and other assets have been bequeathed to the legal heirs, including SV.”

14. It is clear from the said recitals that the petitioners were fully aware that the Companies were controlled and managed by Sh Ashok Varma, his widow and their two daughters. It is also clear that the petitioners were aware that there were certain differences between the family members arising out of a Will and discussions were being held to resolve the *inter se* disputes. It is also clear that Ms Shefali Varma

had represented that a family settlement would be executed. The recitals also record her express representation that she and no other legal heir would be entitled and empowered to deal with the land owning companies (the Companies) and the land after signing of the family settlement.

15. Given the recitals recorded in the agreements in question and considering that it was known to the petitioners that the entire share capital of the Companies was held, either directly or indirectly, by late Sh Ashok Varma and there were difference among the family members with regard to the bequest of his assets; the contention that the petitioners had no occasion to make enquires as to the authority of Ms Shefali Varma to enter into the Agreement, cannot be accepted. The petitioners could not, in these circumstances, proceed on the assumption that Ms Shefali Varma was duly authorized by the Board of Directors of the Companies to enter into the Agreement, without a copy of such resolution(s) being made available to them.

16. It is also contended on behalf of the petitioners that a due diligence exercise was carried out in the offices of the Companies. It is rudimentary for such exercise to entail examination of the books of the company and the same would have revealed whether there was any corporate authority in favour of Ms Shefali Varma, authorizing her to enter into any agreement on behalf of the Companies. Admittedly, Ms Shefali Varma did not furnish copy of any resolution(s) of the Companies authorizing her to enter into the Agreement. Further, it could not be assumed that she was authorized to enter into agreements

dealing with the substantial assets of the Companies solely for the reasons that she was one of the Directors of the Companies.

17. Curiously, the consideration paid by the petitioners was also not paid directly to the Companies but to Ms Shefali Varma personally. Ms Shefali Varma had not produced any resolution of the Companies authorizing her to receive funds on behalf of the Companies in her own name. Admittedly, the Articles of Association of the Companies also do not empower any of their respective directors to receive funds on their behalf directly in their name. There is also no material to suggest that such a practice was common to the trade.

18. In the given facts, this Court is unable to accept that the doctrine of indoor management is applicable.

19. The doctrine of indoor management is also commonly known as Turquand's rule, as it was first enunciated in the case of ***Royal British Bank vs Turquand: 1856 (6E&B) 327***. In that case, the Charter of the company allowed the directors to borrow on bond such sums of money, as required from time to time, by a resolution passed by a General Body Meeting of the company. Such a resolution was passed; however, the amounts were not specified. The company had executed a bond, which was signed by two directors and secretary and was given under seal of the company to Royal British Bank to secure drawings on its current account. In an action instituted on the said bond, the company contested the same by pleading that since a specific resolution had not been passed by the company, it was not

required to make payment to the bank. The Court of Exchequer rejected the said contention and held that the company was bound by the Bond. The relevant extract of the said decision is quoted below:-

“The deed allows the directors to borrow on bond such sum or sums of money as shall from time to time, by a resolution passed at a general meeting of the company, be authorised to be borrowed : and the replication shows a resolution passed at a general meeting, authorising the directors to borrow on bond such sums for such periods and at such rates of interest as they might deem expedient, in accordance with the deed of settlement and Act of Parliament; but the resolution does not define the amount to be borrowed. That seems to me enough.....We may now take for granted that the dealings with these companies are not like dealings with other partnerships, and the parties dealing with them are bound to read the statute and the deed of settlement. But they are not bound to do more.

And the party here on reading the deed of settlement, would find, not a prohibition from borrowing but a permission to do so on certain conditions. Finding that the authority might be made complete by a resolution, he would have a right to infer the fact of a resolution authorising that which on the face of the document appear to be legitimately done.”

20. It is seen from the above that the necessary documents to establish that the persons executing the Bond were authorized to do so had been produced. Not only did the Charter of the company (deed of settlement) empower the directors to borrow money, but a resolution authorizing them to do so was also filed. It is in this context that the court had enunciated the doctrine of indoor management. A person

dealing with a company, who has taken all reasonable steps to satisfy himself that the transaction is an authorized one, is entitled to assume that all internal proceedings of the company would have been duly complied with.

21. It is well accepted that the doctrine of indoor management has limited application and a person who has either a constructive or actual notice of any irregularity, cannot seek protection under the doctrine of indoor management. This doctrine would also have little application in cases of fraud and forgery. Similarly, in cases where a person dealing with a company could discover the irregularities by making inquiries that are normally expected to be made before entering into such transactions, cannot seek recourse of doctrine of indoor management if he has acted negligently and not made the inquiries that are normally made in such cases. Transactions, which are beyond the scope of the apparent authority of the person entering into the transaction on behalf of the company, are also not binding on the company.

22. In ***MRF Ltd v. Manohar Parrikar: (2010) 11 SCC 374***, the Supreme Court observed as under:-

“111. The doctrine of indoor management is in direct contrast to the doctrine or rule of constructive notice, which is essentially a presumption operating in favour of the company against the outsider. It prevents the outsider from alleging that he did not know that the constitution of the company rendered a particular act or a particular delegation of authority ultra vires. The doctrine of indoor management is an

exception to the rule of constructive notice. It imposes an important limitation on the doctrine of constructive notice. According to this doctrine, persons dealing with the company are entitled to presume that internal requirements prescribed in the memorandum and articles have been properly observed. Therefore, doctrine of indoor management protects outsiders dealing or contracting with a company, whereas doctrine of constructive notice protects the insiders of a company or corporation against dealings with the outsiders. However, suspicion of irregularity has been widely recognized as an exception to the doctrine of indoor management. The protection of the doctrine is not available where the circumstances surrounding the contract are suspicious and therefore invite inquiry.

112. This exception was highlighted in the English case of *Houghton & Co. v. Nothard, Lowe & Wills Ltd.*, where the case involved an agreement between fruit brokers and fruit importing company. There was an allegation that the agreement was entered into by the company's directors without authority. It was held that the nature of transaction was found to have been such as to put the plaintiffs on inquiry. To this effect Sargant, L.J. held: (KB p. 267)

“Cases where the question has been as to the exact formalities observed when the seal of a company has been affixed, such as *Royal British Bank v. Turquand* or *County of Gloucester Bank v. Rudry Merthyr Steam and House Coal Colliery Co.*, are quite distinguishable from the present case. In *Fireproof Doors Ltd.*, In re, tends rather against than in favour of the plaintiffs, since if a single director has as towards third parties the authority now contended for, the whole of the elaborate investigation of the

facts in that case was entirely unnecessary. Perhaps the nearest approach to the present case is to be found in *Biggerstaff v. Rowatt's Wharf Ltd.* But there the agent whose authority was relied on had been acting to the knowledge of the company as a managing director, and the act done was one within the ordinary ambit of the powers of a managing director in the transaction of the company's affairs. It is, I think, clear that the transaction there would not have been supported had it not been in this ordinary course or had the agent been acting merely as one of the ordinary directors of the company. I know of no case in which an ordinary director, acting without authority in fact, has been held capable of binding a company by a contract with a third party, merely on the ground that that third party assumed that the director had been given authority by the Board to make the contract. A limitation of the right to make such an assumption is expressed in Buckley on the Companies Acts, 10th Edn., p. 175, in the following concise words: 'And the principle does not apply to the case where an agent of the company has done something beyond any authority which was given to him or which he was held out as having.'"

113. This exception to the doctrine of indoor management has been subsequently adopted in many Indian cases. They are *B. Anand Behari Lal v. Dinshaw and Co. (Bankers) Ltd.* and *Abdul Rahman Khan v. Mufassal Bank Ltd.* Applying the exception to the present scenario, there is sufficient doubt with regard to the conduct of the Power Minister in issuing the Notifications dated 15-5-1996 and 1-8-1996. Therefore, there is a definite suspicion of

irregularity which renders the doctrine of indoor management inapplicable to the present case.”

23. In the present case, the circumstances clearly warranted the petitioners to ascertain whether Ms Shefali Varma had the requisite authority to act on behalf of the Companies. The subject matter of the Agreement was a land owned by the Companies. As noticed above, the recitals of the agreements in question clearly indicated that Ms Shefali Varma did not have the authority to deal with the land in question. She was expecting that she would secure such authority as and when the family settlement was entered into.

24. Almost the entire shareholding of the Companies was held, either directly or indirectly, by late Sh Ashok Varma. It is also not disputed that none of the shares held by him were transmitted to the petitioners in the records of the Companies. It is also not disputed that there is no provision in the Articles of Association, which empowers a Director of the Companies to singly deal with the properties of the company. Thus, the petitioners had constructive notice that a specific resolution authorizing the petitioners was necessary to enable Ms Shefali Varma to enter into the Agreement. More importantly, the petitioners were aware that the Companies were closely held companies of the Varma Family and there were disputes and differences between them. Plainly, in such circumstances, the doctrine of indoor management is inapplicable.

25. The petitioners have been unable to produce any resolution or to controvert the stand of the Companies that they had not passed any

resolution(s) authorizing Ms Shefali Varma to enter into the Agreement. Thus, it is difficult to accept that the Agreement is binding on the Companies. Consequently, this Court cannot accept that an arbitration agreement exists between the Companies and the petitioners.

26. Insofar as Ms Shefali Varma is concerned, there can be no dispute that an arbitration agreement exists between the petitioners and her. There is no dispute that she has executed the Agreement. The Agreement contains an arbitration clause. It is also trite that an arbitration clause constitutes a separate agreement independent of the main agreement. Thus, notwithstanding any contention raised by Ms Shefali Varma regarding the nature and validity of the Agreement, there is no doubt that the arbitration clause is binding between the petitioners and Ms Shefali Varma.

27. The disputes arising between the said parties – that is, the petitioners and Ms Shefali Varma – in connection with the Agreement are required to be referred to arbitration.

28. In view of the above, Mr. Justice Badar Durrez Ahmed, Former Chief Justice, Jammu & Kashmir High Court (Mobile No. 7042205786) is appointed as a sole arbitrator to adjudicate the disputes between the petitioners and Ms Shefali Varma. This is subject to the Arbitrator furnishing the necessary disclosure as required under Section 12 of the A&C Act and not being ineligible under Section

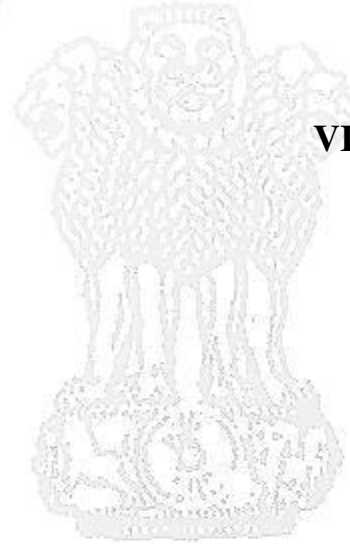
12(5) of the A&C Act. The Arbitrator shall fix his fees in consultation with the parties.

29. The parties are at liberty to approach the Arbitrator for further proceedings.

30. The petition is allowed in the above terms.

JULY 22, 2019
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VIBHU BAKHRU, J



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