

# Shareholder disputes from a foreign investor perspective

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Investing in India can be challenging, with myriad central and state level laws, as well as cumbersome sector-specific requirements. Often, foreign investors seek relationships with local promoters to overcome these hurdles. However, difficulties increase when investors become embroiled in litigation or arbitration with Indian promoters over issues related to mismanagement, control, earn-out payments etc. Disputes that arise between the shareholders generally fall into three categories – contractual disputes arising from shareholder or joint venture agreements, oppression and mismanagement issues and criminal matters.



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Contractual disputes. Arbitration is the most popular dispute resolution mechanism for the resolution of issues arising from shareholder agreements. The contractual rights of investors are best protected when highly qualified arbitrators, preferably of a neutral nationality, conduct international commercial arbitrations in accordance with time-bound arbitration rules. The choice of the seat of arbitration also plays a key role. To avoid difficulties in the enforcement of foreign awards, investors should choose countries that have been notified by the Government of India as territories having reciprocal provisions for enforcement of Indian awards. Unlike awards from reciprocating jurisdictions, which can be executed straight away, the execution of awards of non-reciprocating jurisdictions is cumbersome and expensive as the award-holder must start a civil action in India based on the award and obtain an execution order.

Some of the most hard-fought contractual disputes between shareholders are in relation to earn-out payments. Earn-out is a contractual provision for the seller to receive further compensation if certain metrics, generally financial, are met in the future. It is used where there is a gap between buyer and seller in the perceived value of a company. The earn-out allows the transaction to take place and bridges the gap between the parties' expectations of the value of the company, allowing the buyer to pay only for a successful business. To avoid disputes on the valuation of an earn-out, the contractual terms must be clearly defined and unambiguous. It is important for the buyer and seller to agree on a business plan and the level of input that the seller will retain following the investment or acquisition. This input can include protection and veto rights pertaining to the management of the business going forward.

Oppression and mismanagement issues. These disputes generally relate to matters such as the exercise of undue control, denial of access to company information and oppressive conduct. There have been several instances of promoters continuing to exercise control and direct the policies of joint venture companies despite divesting a majority stake. Japanese investors in particular are prone to such risks given their inclination to have Japanese expats in senior management roles, at least in the early stages of the joint venture investment. Foreigners' lack of familiarity with local laws gives Indian promoters the opportunity to remain in control. Frequently, these conflicts spiral into serious disputes. These matters contravene the [Companies Act, 2013](#), and must be brought before the [National Company Law Tribunal](#). However, care must be taken to separate contractual issues. The application must not be a dressed-up petition for the adjudication of issues that should be determined in arbitration.

Criminal matters. An increasing number of criminal proceedings are brought against expats by joint venture companies as a bargaining tool. To mitigate their exposure, foreign investors must conduct thorough due diligence not only on target companies but also on the backgrounds and reputations of prospective joint venture partners. Foreign investors, especially Japanese investors, who often hire expats for key management positions, should recruit reliable local key managerial personnel to handle practical challenges and mitigate daily compliance risk.

With the right advice, the risks faced by foreign investors can be mitigated, and a strategy devised for efficiently handling, or even avoiding, shareholder disputes.

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