> Perhaps another (and simpler) way of putting the matter is that a director is an agent, who casts his vote to decide in what manner his principal shall act through the collective agency of the board of directors; a shareholder who casts his vote in general meeting is not casting it as an agent of the company in any shape or form. His act therefore, in voting as he pleases, cannot in any way be regarded as an act of the company …
>
> I now come to paragraph 4 of the notice of motion, which seeks an order restraining the individual respondents [ie the directors] and each of them from voting against the resolution. Mr Price says that, as the executive agents of the defendant company, they are bound to recommend to its shareholders that they vote in favour of the resolution to issue the shares, and hence, at the least, they cannot themselves vote against it, for they would thereby be assisting the defendant company to do that which it is their duty to secure does not happen. If, as executive officers of the defendant company, they are bound to procure a certain result if at all possible, how can they, as individuals, seek to frustrate that result?
>
> I regret, however, that I am unable to accede to Mr Price's arguments in this respect … I think that a director who has fulfilled his duty as a director of a company, by causing it to comply with an undertaking binding upon it is nevertheless free, as an individual shareholder, to enjoy the same unfettered and unrestricted right of voting at general meeting of the members of the company as he would have if he were not also a director …

(p. 216) See also *Pender v Lushington* **[13.19]**; *North-West Transportation Co Ltd v Beatty* **[4.33]**; *Burland v Earle* [1902] AC 83, PC; and *Peter's American Delicacy Co Ltd v Heath* **[4.26]**.

➢ Notes

1. *Halton International Inc (Holdings) Sarl v Guernroy Ltd* [2005] EWHC 1968 (Ch) reinforces this finding. The defendant, a member of the company, was given the power to exercise the votes of all other members for the purpose of raising fresh capital in any way he saw fit. The defendant member passed a resolution suspending the pre-emption rights of the other members which were inserted in the company articles, thereby increasing his voting rights in the selection of investors. The court held that the voting agreement did not give rise to any fiduciary duties on the part of the acting member. His actions were authorised by the agreement and were therefore upheld.

2. Similarly, in *McKillen v Misland (Cyprus) Investments Ltd & Ors* [2012] EWHC 521 (Ch), the court rejected an attempt to interpret a shareholders' agreement in a way which would impose fiduciary duties on shareholders.

3. The rule that a member owes no duties to the company and can exercise his rights entirely as he pleases, without regard to the effect of doing so upon the company, is not confined to the right to vote. In *Stothers v William Steward (Holdings) Ltd* [1994] 2 BCLC 266 it was applied to the right of a member (subject, of course, to any provision in the articles) to transfer his shares to a person of his choice. But where the articles do make special provision, the outcome may be different: see *Cream Holdings Ltd v Stuart Davenport* [2010] EWHC 3096 (Ch), in Note 4 following *Equitable Life Assurance Society v Hyman* **[4.03]**, p 186.

4. By contrast, and quite exceptionally, the courts have on rare occasions been prepared to order that a member's votes should be cast, or at least not cast, in a certain way—in effect, to restrain him from acting perversely.

In *Standard Chartered Bank Ltd v Walker* [1992] 1 WLR 561, a member with a minority holding of shares was ordered not to vote against a restructuring agreement where the consequence of his doing so would have been that the company would collapse and his shares (which had been charged to the company's banks) would become worthless.

Similarly, in *Theseus Exploration NL v Mining & Associated Industries Ltd* [1973] Qd R 81 an injunction was

granted against majority members restraining them from voting to remove the existing directors and replace them with a board intent on a policy of destructive asset-stripping.

More recently, in a case before the Companies Court of the Hong Kong Court of First Instance, Harris J granted an injunction to restrain the defendant shareholders from voting against a restructuring proposal which, if exercised, would 'result in the destruction of the economic value of other shareholders' shares for no rational reason' [33]: *Sunlink International Holdings Ltd v Wong* [2010] 5 HKLRD 653, HCA 1527/2010. It has been suggested, however, that the 'no rational basis' test in this case is too general, and requires further refinement and clarification by a higher court when the opportunity arises: William MF Wong, 'Can Shareholders Vote Irrationally?' (2011) LQR 522.

➢ Question

How, if at all, can these cases be seen as consistent with cases that seem to impose restrictions on members when voting to alter the articles, or members when voting to alter class rights (see 'Alteration of the articles', pp 219ff and 'Variation of class rights', pp 563ff)?

(p. 217) ***A contract by a member to vote in a particular way, or as directed by another person, is binding and may be enforced by a mandatory injunction.***[31]

[4.19] Puddephatt v Leith [1916] 1 Ch 200 (Chancery Division)

The plaintiff had mortgaged shares in the company to the defendant and transferred them into his name. By a contemporaneous letter, the defendant had undertaken to vote the shares as directed by the plaintiff. The court ordered him to comply with the undertaking.

> SARGENT J [after stating the facts and holding that the undertaking to vote in accordance with the plaintiff's wishes contained in the letter constituted a collateral agreement binding on the defendant, continued]: In my opinion, therefore, the right of the plaintiff is clear, and the only remaining question is whether she is entitled to a mandatory injunction to enforce her right. It is not disputed that she is entitled to a prohibitive injunction, and in my opinion she is also entitled to a mandatory injunction. Prima facie this court is bound … to give effect to a clear right by way of a mandatory injunction. There are no doubt certain exceptions from this rule, as in the case of a contract of service, because in such cases, it is impossible for the court to make its order effective, but … in the present case, in as much as there is one definite thing to be done, about the mode of doing which there can be no possible doubt, I am of opinion that I ought to grant not only the prohibitive but also the mandatory injunction claimed by the plaintiff, and I make an order accordingly.

➢ Notes

1. The specific undertaking given in this case displaced the normal rule that a mortgagee of shares may exercise the voting rights in respect of those shares free of any dictation from the mortgagor: *Siemens Bros & Co Ltd v Burns* [1918] 2 Ch 324, CA; *Stablewood Properties Ltd v Virdi* [2010] EWCA Civ 865, CA. Similarly, an *unpaid*vendor of shares who remains on the share register retains the voting rights free from dictation by the purchaser (*Musselwhite v CH Musselwhite & Son Ltd* [1962] Ch 964), although (at least where the contract is specifically enforceable) these rights may be inhibited by a fiduciary obligation to have regard to the purchaser's interests (*Michaels v Harley House (Marylebone) Ltd* [2000] Ch 104, CA). But once the purchaser has paid the full price, the vendor holds the shares as a bare trustee (*Hawks v McArthur* **[11.18]**), and must vote the shares as directed by the purchaser (*Re Piccadilly Radio plc* [1989] BCLC 683).

2. This case concerned a single shareholder. A contract between several shareholders, agreeing to coordinate their votes, or delegating to one the power to cast votes for all—commonly known as 'voting trust'—is lawful. It is more widely used in the United States than in the UK, and can be a powerful tool either to concentrate control behind the management, or to use as a countervailing force against it.[32]

A decision carried by the votes of majority members may be set aside if it is 'oppressive' of the minority.

[4.20] Clemens v Clemens Bros Ltd [1976] 2 All ER 268 (Chancery Division)

The plaintiff held 45% and her aunt ('Miss Clemens') 55% of the shares in the defendant company. The company's articles gave existing members a pre-emptive right if another member **(p. 218)** wished to transfer his shares. The plaintiff therefore had an expectation of total control of the company after her aunt's death, and 'negative control' (ie the power to block a special resolution) in the aunt's lifetime. The aunt and four non-shareholders were the directors. The directors proposed that the company's capital should be increased by issuing 200 ordinary shares to each of these four directors, and 850 ordinary shares to an employees' trust; and resolutions to this effect were passed by the aunt's votes at a general meeting. Although it was claimed that the object of the resolutions was in the company's interests (namely, to give the directors and employees a stake in the company) the court took the view that the real object was to deprive the plaintiff of her degree of control, and the resolutions were set aside.

FOSTER J: For the plaintiff it was submitted that the proposed resolutions were oppressive, since they resulted in her losing her right to veto a special or extraordinary resolution and greatly watered down her existing right to purchase Miss Clemens' shares under article 6. For the defendants it was submitted that if the two shareholders both honestly hold differing opinions, the view of the majority must prevail and that the shareholders in general meeting are entitled to consider their own interests and vote in any way they honestly believe proper in the interests of the company.

There are many cases which have discussed a director's position. A director must not only act within his powers but must also exercise them bona fide in what he believes to be the interests of the company. The directors have a fiduciary duty, but is there any similar, restraint on shareholders exercising their powers as members at general meetings? [His Lordship read extracts from the judgments in a number of cases, including *Greenhalgh v Arderne Cinemas* **[4.27]**,[33] and continued:]

I think that one thing which emerges from the cases to which I have referred is that in such a case as the present Miss Clemens is not entitled to exercise her majority vote in whatever way she pleases. The difficulty is in finding a principle, and obviously expressions such as 'bona fide for the benefit of the company as a whole', fraud on a 'minority' and 'oppressive' do not assist in formulating a principle.

I have come to the conclusion that it would be unwise to try to produce a principle, since the circumstances of each case are infinitely varied. It would not, I think, assist to say more than that in my judgment Miss Clemens is not entitled as of right to exercise her votes as an ordinary shareholder in any way she pleases. To use the phrase of Lord Wilberforce,[34] that right is 'subject … to equitable considerations … which may make it unjust … to exercise [it] in a particular way'. Are there then any such considerations in this case?

I do not doubt that Miss Clemens is in favour of the resolutions and knows and understands their purport and effect; nor do I doubt that she genuinely would like to see the other directors have shares in the company and to see a trust set up for long service employees. But I cannot escape the conclusion that the resolutions have been framed so as to put into the hands of Miss Clemens and her fellow directors complete control of the company and to deprive the plaintiff of her existing rights as a shareholder with more than 25% of the votes and greatly reduce her [pre-emptive] rights … They are specifically and carefully designed to ensure not only that the plaintiff can never get control of the company but to deprive her of what has been called her negative control. Whether I say that these proposals are oppressive to the plaintiff or that no one could honestly believe they are for her benefit matters not. A court of equity will in my judgment regard these considerations as sufficient to prevent the consequences arising from Miss Clemens using her legal right to vote in the way that she has and it would be right for a court of equity to prevent such

consequences taking effect.

➢ Note

This case may have reached a just result on the merits (although that has been doubted, for there was a long history of non-cooperation by the niece), but the judge's use of the authorities **(p. 219)** contrasts with earlier approaches. The citation of *Greenhalgh* **[4.27]** draws on a line of decisions concerned with special resolutions for the alteration of articles, which had never before been applied to other types of resolution. Further, having read the passage from *Greenhalgh*'s case in which Evershed MR suggested the test of the 'individual hypothetical shareholder', Foster J commented: 'If that is right, the question in the instant case must be posed thus: did Miss Clemens, when voting for the resolutions, honestly believe that those resolutions, when passed, would be for the benefit of the plaintiff?' It might equally be observed that the plaintiff was no more a hypothetical shareholder than Miss Clemens herself; and if the test had been understood in this sense in *Greenhalgh*'s case itself, the decision must surely have gone in Greenhalgh's favour. These cases show how unhelpful the 'hypothetical shareholder' test is, especially in regard to small companies. And, in quoting Lord Wilberforce, the judge is again borrowing, this time from the winding-up cases, a borrowing which might be seen as contrary to the ruling in*Bentley-Stevens v Jones* [1974] 1 WLR 639.

➢ Questions

1. Did Foster J consider that a member in the position of Miss Clemens was under a duty to (i) the company, or (ii) her fellow-shareholder? If so, what was the nature of this duty? If not, what was the rule or principle which he was applying?

2. If the aunt did owe such a duty, did the niece owe the company, or her fellow-shareholder, any corresponding duty?

3. Can the *Clemens* and *Greenhalgh* **[4.27]** cases be reconciled?

Alteration of the articles

CA 2006 s 21: alteration of articles

Provisions in the company's articles can be amended by special resolution (s 21), unless they have been entrenched under s 22.[35] Section 22 allows the articles to contain a '*provision for entrenchment*' nominating specified provisions of the articles that can be amended or deleted only if conditions or procedures more stringent than a special resolution are met. Note that CA 2006 s 22(2) has not been brought into force (see 'History', p 25).

If such a provision for entrenchment was contained in the company's old-style memorandum, it will automatically be treated as part of the company's articles under the new legislation (s 28(2)), so the entrenchment will be preserved. Notice of the existence, amendment or deletion of provisions of entrenchment must be given to the Companies House (s 23, and s 13 for the 'form of compliance').

CA 2006 s 25 retains the principle that a member of a company is not bound by any alteration made to the articles after he or she becomes a member if the alteration has the effect of increasing liability to the company or imposing a requirement to take more shares in the company. A member may, however, give written consent to such an alteration and, in that case, will be bound by it.

Earlier case law thus remains relevant.

Predecessor provisions

Until CA 2006 came into force, companies were required to have both a *memorandum and articles* (see 'Capacity: what is a company legally entitled to do', p 85). There were different **(p. 220)** statutory rules for altering each of them. Indeed, when the memorandum of association was first introduced as the basic constitutional document of a company by the Joint Stock Companies Act 1856, none of its provisions could be altered (apart from the capital clause pursuant to an increase of capital). Over time, the position was reached under CA 1985 where it was possible to alter any of the clauses of the memorandum, except that fixing the company's domicile, by the use of the appropriate procedure. The company's name could be changed under CA 1985 s 28, the objects clause under s 4, the company's status as limited or unlimited, public or private, and so on, by the various procedures set out in Pt II of the Act, and the capital provisions under CA 1985 ss 121, 125 and 135.

The alteration of a company's objects (see 'Capacity: what is a company legally entitled to do', p 85), contained in the memorandum, required a special resolution, and the court became involved only if the holders of 15% or more of the issued share capital of any class made an objection by applying to the court within 21 days. The court then had an absolute discretion to confirm or disallow the alteration. It is perhaps significant that the only reported cases on the exercise of the court's discretion, under both the 1985 Act and previous procedures, seem to have been concerned with non-commercial organisations. See *Re Cyclists' Touring Club* [1907] 1 Ch 269 and *Re Hampstead Garden Suburb Trust Ltd* [1962] Ch 806.

By contrast, the Acts had always allowed the articles to be altered by special resolution, with no statutory constraints except for the protection given by CA 1985 s 125 in relation to variation of 'class rights'.[36] (See 'Variation of class rights', pp 563ff.)

With these bald requirements set by statute, judges have been left with the task of formulating more specific rules controlling the power of majority members to alter articles. Unfortunately the principles that have emerged are anything but clear. As a rule, the courts have been content to fall back on such broad general phrases as 'bona fide for the benefit of the company as a whole', apparently without appreciating that these expressions mask rather than explain the decisions they are making. The difficulty posed by the juxtaposition of the 'benefit of the company' test with the basic concept of the member's vote as a property right is all too rarely faced in the judgments (with the notable exception of *Peter's American Delicacy Co Ltd v Heath* **[4.26]**). If it had been, the cases that follow might have yielded more intelligible principles.

A contract by a company not to alter its articles will not be enforced by injunction.

[4.21] Punt v Symons & Co Ltd [1903] 2 Ch 506 (Chancery Division)

By arts 95 and 97 of the defendant company's articles GG Symons, as governing director, was given the power to appoint and remove directors, and after his death the same power was exercisable by his executors. The company had also agreed in a separate contract, relating to the purchase of Symons's business, that it would not alter these articles. After the death of Symons, friction arose between his executors and the directors, which led to a proposal from the directors to rescind the articles in question by special resolution. The executors moved for an injunction.[37]

> BYRNE J: The first point taken is that passing the resolution would be a breach of the contract which was entered into with the testator; and that the plaintiffs as executors are entitled to enforce the terms of the agreement by restraining any alteration of the articles. I think the answer to this **(p. 221)** argument is—that the company cannot contract itself out of the right to alter its articles, though it cannot, by altering its articles, commit[38] a breach of contract. It is well established as between a company and a shareholder, the right not depending upon a special contract outside the articles, that this is the case. It has not been, so far as I know, the precise subject of reported decision as between a contractor and a company where the contract is independent of and outside the articles … [His Lordship referred to *Allen v Gold Reefs of West Africa* **[4.22]**; and to an unreported decision *Re Ladies' Dress Association Ltd*, in which a contract not to alter any article was not enforced. He continued:] That appears, so far as I can judge, to be a decision upon the point now before me. Whether that be so or not, I am prepared to hold that in the circumstances of

the present case the contract could not operate to prevent the article being altered under the provisions of s 50 of the Companies Act 1862 [CA 2006 s 21], whatever the result of that alteration may be.

See also *Baily v British Equitable Assurance Co* **[3.18]** and *Southern Foundries (1926) Ltd v Shirlaw* **[6.04]**.

➢ Notes

1. The opinion expressed in this case is supported by the emphatic *obiter dictum* of Lord Porter in *Southern Foundries (1926) Ltd v Shirlaw* **[6.04]**. It is therefore to be preferred, it is submitted, to the contrary view of Sargant J in *British Murac Syndicate Ltd v Alperton Rubber Ltd* [1915] 2 Ch 186, which was based on the mistaken view that *Punt*'s case had been overruled by *Baily v British Equitable Assurance Co* **[3.18]**.

2. However, it does not follow that a contractual undertaking by a company that its articles will not be altered might not be enforced in other ways. Lord Porter clearly thought that, if a company *acted upon* its altered articles in a way which was in breach of an existing contract, a remedy in damages would lie. In principle, this must be correct; and further, in principle also, an injunction might in such circumstances be granted, in the discretion of the court, restraining the company from acting upon its altered articles.

3. As Byrne J notes, it was already a well-established rule that a company could not restrict the right to alter its articles by a provision in the articles themselves. This was decided by Jessel MR in *Walker v London Tramways Co* (1879) 12 Ch D 705, where he held that a provision in the company's articles declaring that certain articles were 'essential' and unalterable was ineffective.

4. This ruling is but one illustration of a more general principle that a company cannot bargain away its right to exercise the powers conferred upon it by statute. The extent to which there is such a rule, and (assuming that there is) whether there ought to be such a rule, was a matter of considerable debate, following the decision in*Russell v Northern Bank Development Corpn Ltd* **[4.34]** (see Sealy [1992] CLJ 437). There is clear authority establishing that a company cannot contract not to alter its articles (*Punt*'s case, Note 1) nor contract not to alter its capital (*Russell*). This principle would surely also extend to such matters as contracting not to go into liquidation or to petition for a winding-up order. But it is easy to demonstrate that there may be good commercial reasons why a company might wish to bind itself not to do at least some of these things—for instance, a bank lending money to a company may make it a condition of the loan that the company will not reduce its capital—and, indeed, this has been done in practice for many years. So, following the ruling in *Russell*, there has been pressure for Parliament to change the law so as to make contractual undertakings given in such circumstances binding. The case for retaining a general principle of this kind is greatly weakened by the fact that there are many alternative ways of doing indirectly what cannot at present be achieved directly—for example, by a shareholder agreement ('Shareholders' agreements', p 244), by attaching 'class **(p. 222)** rights' to certain shares (see the *Cumbrian Newspapers* case **[11.05]**, by entrenching the rights which it is sought to protect in the old-style memorandum (see CA 1985 s 17(2)(b)) or, now, in the articles (see CA 2006 s 22), or by the use of 'weighted' voting rights (see *Bushell v Faith* **[6.02]**). And, in the example of the bank loan, the bank could stipulate that the money would become immediately repayable if the company should summon a general meeting to consider a proposed resolution to reduce capital.

5. Finally, note that all these limitations apply to the *company* limiting its statutory rights. The shareholders, by contrast, can agree amongst themselves via a shareholder agreement, not to alter the company's articles, or not to do any manner of other things. But would a shareholder agreement not to alter the company's articles ever be *specifically enforced*, or would it only give rise to damages for breach? (See 'Shareholders' agreements', pp 244ff.)

➢ Question

In *Walker v London Tramways* Co (see earlier), Jessel MR did not give a reasoned judgment but simply asserted that no company could contract itself out of CA 1962 s 50 (the equivalent of CA 2006 s 21). What reasoning do you think that he might have used, and would you agree?

The power to alter a company's articles must be exercised 'bona fide for the benefit of the company as a whole'. An alteration so made is valid and binding on the members and may affect their existing rights as members. It may, however, amount to a breach of an independent contract.

[4.22] Allen v Gold Reefs of West Africa Ltd [1900] 1 Ch 656 (Court of Appeal)

Article 29 of the company's articles of association gave it 'a first and paramount lien' for debts owing by a member to the company 'upon all shares (not being fully paid) held by such members'. The company altered this article by deleting the words 'not being fully paid'. Only one shareholder, Zuccani (who had died insolvent), was affected by this alteration: he had had fully paid shares allotted to him when the company was formed, and had later acquired other shares, that were not fully paid, on which calls were overdue. His executors challenged the company's right to claim a lien on his fully paid shares pursuant to the altered article. Kekewich J held that the company could not enforce its lien. The Court of Appeal reversed this decision, and upheld the alteration.

> LINDLEY MR: The articles of a company prescribe the regulations binding on its members: Companies Act 1862, s 14 [CA 2006 s 21]. They have the effect of a contract (see s 16 [CA 2006 s 33]); but the exact nature of this contract is even now very difficult to define. Be its nature what it may, the company is empowered by the statute to alter the regulations contained in its articles from time to time by special resolutions (ss 50 and 51 [CA 2006 ss 21, 283]); and any regulation or article purporting to deprive the company of this power is invalid on the ground that it is contrary to the statute: *Walker v London Tramways Co*.[39]
>
> The power thus conferred on companies to alter the regulations contained in their articles is limited only by the provisions contained in the statute and the conditions contained in the company's memorandum of association. Wide, however, as the language of s 50 is, the power conferred by it must, like all other powers, be exercised subject to those general principles of law and equity which are applicable to all powers conferred on majorities and enabling them to bind minorities. It must be **(p. 223)** exercised, not only in the manner required by law, but also bona fide for the benefit of the company as a whole, and it must not be exceeded. These conditions are always implied, and are seldom, if ever, expressed. But if they are complied with I can discover no ground for judicially putting any other restrictions on the power conferred by the section than those contained in it. How shares shall be transferred, and whether the company shall have any lien on them, are clearly matters of regulation properly prescribed by a company's articles of association. This is shown by Table A in the Schedule to the Companies Act … Speaking, therefore, generally, and without reference to any particular case, the section clearly authorises a limited company, formulated with articles which confer no lien on fully paid-up shares, and which allow them to be transferred without any fetter, to alter those articles by special resolution, and to impose a lien and restrictions on the registry of transfers of those shares by members indebted to the company.
>
> But then comes the question whether this can be done so as to impose a lien or restriction in respect of a debt contracted before and existing at the time when the articles are altered. Again, speaking generally, I am of opinion that the articles can be so altered, and that, if they are altered bona fide for the benefit of the company, they will be valid and binding as altered on the existing holders of paid-up shares, whether such holders are indebted or not indebted to the company when the alteration is made. But, as it will be seen presently, it does not by any means follow that the altered article may not be inapplicable to some particular fully paid-up shareholder. He may have special rights against the company, which do not invalidate the resolution to alter the articles, but which may exempt him from the operation of the articles as altered.
>
> But, although the regulations contained in a company's articles of association are revocable by special resolution, a special contract may be made with the company in the terms of or embodying one or more of

the articles, and the question will then arise whether an alteration of the articles so embodied is consistent or inconsistent with the real bargain between the parties. A company cannot break its contracts by altering its articles,[40] but, when dealing with contracts referring to revocable articles, and especially with contracts between a member of the company and the company respecting his shares, care must be taken not to assume that the contract involves as one of its terms an article which is not to be altered.

It is easy to imagine cases in which even a member of a company may acquire by contract or otherwise special rights against the company, which exclude him from the operation of a subsequently altered article. Such a case arose in *Swabey v Port Darwin Gold Mining* **[6.03]** where it was held that directors, who had earned fees payable under a company's articles, could not be deprived of them by a subsequent alteration of the articles, which reduced the fees payable to directors.

I take it to be clear that an application for an allotment of shares on the terms of the company's articles does not exclude the power to alter them nor the application of them, when altered, to the shares so applied for and allotted. To exclude that power or the application of an altered article to particular shares, some clear and distinct agreement for that exclusion must be shown, or some circumstances must be proved conferring a legal or equitable right on the shareholders to be treated by the company differently from the other shareholders.

This brings me to the last question which has to be considered, namely, whether there is in this case any contract or other circumstance which excludes the application of the altered article to Zuccani's fully paid-up vendor's shares. [His Lordship ruled that there was no such special circumstance, and continued:]

The fact that Zuccani's executors were the only persons practically affected at the time by the alterations made in the articles excites suspicion as to the bona fides of the company. But, although the executors were the only persons who were actually affected at the time, that was because Zuccani was the only holder of paid-up shares who at the time was in arrear of calls. The altered **(p. 224)** articles applied to all holders of fully paid shares, and made no distinction between them. The directors cannot be charged with bad faith.

After carefully considering the whole case, and endeavouring in vain to discover grounds for holding that there was some special bargain differentiating Zuccani's shares from others, I have come to the conclusion that the appeal from the decision of the learned judge, so far as it relates to the lien created by the altered articles, must be allowed …

ROMER LJ delivered a concurring judgment.

VAUGHAN WILLIAMS LJ dissented.

[4.23] Sidebottom v Kershaw, Leese & Co Ltd [1920] 1 Ch 154 (Court of Appeal)

The defendant company had altered its articles by introducing a provision which gave the directors power to buy out, at a fair price, the shareholding of any member who competed with the company's business. The plaintiffs, who were minority shareholders and who carried on a competing business, unsuccessfully challenged the validity of the alteration.

LORD STERNDALE MR: In my opinion, the whole of this case comes down to rather a narrow question of fact, which is this: When the directors of this company introduced this alteration giving power to buy up the shares of members who were in competing businesses did they do it bona fide for the benefit of the company or not? It seems to me quite clear that it may be very much to the benefit of the company to get rid of members who are in competing business … I think there can be no doubt that a member of a competing business or an owner of a competing business who is a member of the company has a much better chance of knowing what is going on in the business of the company, and of thereby helping his own competition with it, than if he were a non-member; and looking at it broadly, I cannot have any doubt that in a small private company like this the exclusion of members who are carrying on a competing business may

very well be of great benefit to the company. That seems to me to be precisely a point which ought to be decided by the voices of the business men who understand the business and understand the nature of competition, and whether such a position is or is not for the benefit of the company. I think, looking at the alteration broadly, that it is for the benefit of the company that they should not be obliged to have amongst them as members persons who are competing with them in business, and who may get knowledge from their membership which would enable them to compete better.

That brings me to the last point. It is said that that might be so were it not for the fact that the directors and the secretary have said, 'This is directed against Mr Bodden', and therefore it is not done bona fide for the benefit of the company, but it is done to get rid of Mr Bodden.[41] If it were directed against Mr Bodden for any malicious motive I should agree with that—the thing would cease to be bona fide at once; but these alterations are not as a rule made without some circumstances having arisen to bring the necessity of the alteration to the minds of the directors. I do not read this as meaning anything more than this: 'It was the position of Mr Bodden that made us appreciate the detriment that there might be to the company in having members competing with them in their business, and we passed this, and our intention was, if it became necessary, to use it in the case of Mr Bodden; that is what we had in our minds at the time; but we also had in our minds that Mr Bodden is not the only person who might compete, and therefore we passed this general article in order to enable us to apply it in any case where it was for the good of the company that it should be applied.' It is a question of fact. I come to the conclusion of fact to which I think the Vice-Chancellor came, that the directors were acting perfectly bona fide, that they were passing the resolution for the benefit of the company; but that no doubt the occasion of their passing it was because they realised in the person of Mr Bodden that it was a bad thing to have members who were competing with them …

(p. 225) For these reasons I think this is a valid article. I think the alteration was within the competence of the company, and therefore this appeal must be allowed with costs here and below.

WARRINGTON LJ and EVE J delivered concurring judgments.

[4.24] Citco Banking Corporation NV v Pusser's Ltd [2007] UKPC 13, [2007] BCC 205 (Privy Council)

Before the events in issue in this appeal, the company had share capital of $4.4 million divided into 4.4 million class A shares of $1 each, of which 1,673,217 shares (and warrants for another 248,000) had been issued. Each class A share or warrant carried one vote. At an extraordinary general meeting, the company by special resolution amended its articles of association to create 200,000 class B shares, each carrying 50 votes. It also resolved that 200,000 of the class A shares held by the chairman of the company, Mr Charles S Tobias, be converted into class B shares. The resolutions were carried by 1,125,665 votes to 183,000, the dissenting shares all being held by Citco. Citco alleged that the resolutions were invalid because they were passed in the interests of Mr Tobias, to give him indisputable control, and not bona fide in the interests of the company. The trial judge agreed; the Court of Appeal reversed his decision and held the resolutions valid. The Privy Council upheld this finding.

LORD HOFFMANN delivered the judgment of the Privy Council:

12 Section 89 of the Act [broadly equivalent to CA 2006 s 21] contains no qualification of the power of a 75% majority to amend the articles of association. But the courts have always treated the power as subject to implied limitations. The problem has been to say where the line should be drawn. [He then examined the authorities, including *Allen v Gold Reefs of West Africa Ltd* **[4.22]**, *Dafen Tinplate Co Ltd v Llanelly Steel Co (1907) Ltd* **[4.25]**, *Shuttleworth v Cox Bros and Co (Maidenhead) Ltd* **[6.06]**, and continued:]

17 These were cases in which the amendment operated to the particular disadvantage of a minority of shareholders: Mr Zuccani's estate in *Allen's* case and the director whose removal was proposed in *Shuttleworth's* case. But the same principle must apply when an amendment which the shareholders bona fide consider to be for the benefit of the company as a whole also operates to the particular advantage of some shareholders. This is illustrated by *Rights & Issues Investment Trust Ltd v Stylo Shoes Ltd* **[4.28]**, …

18 These principles, together with the proposition that the burden of proof is upon the person who challenges the validity of the amendment (see *Peters' American Delicacy Company Ltd v Heath* **[4.26]**, per Latham CJ at p 482) appear to their Lordships to be clearly settled and sufficient for the purpose of deciding this case. It must however be acknowledged that the test of 'bona fide for the benefit of the company as a whole' will not enable one to decide all cases in which amendments of the articles operate to the disadvantage of some shareholder or group of shareholders. Such amendments are sometimes only for the purpose of regulating the rights of shareholders in matters in which the company as a corporate entity has no interest, such as the distribution of dividends or capital or the power to dispose of shares. In the Australian case of *Peters' American Delicacy Company*, to which reference has been made, the amendment provided that shareholders should thenceforth receive dividends rateably according to the amounts paid up on their shares rather than, as previously, according to the number of shares (fully or partly paid) which they held. It was, as Dixon J pointed out (at p 512), 'inappropriate, if not meaningless' to ask whether the shareholders had considered the amendment to be in the interests of the company as a whole. Some other test of validity is required. In *Greenhalgh v Arderne Cinemas Ltd* **[4.27]**, where the amendment was to remove a pre-emption clause to facilitate a sale of control to a third party, Sir Raymond Evershed MR tried to preserve the application of the traditional test by saying that in such cases 'the company as a whole' did not mean the company as a corporate entity but 'the corporators as a general body' and that it was necessary to ask whether the amendment was, in the honest opinion of those who voted in favour, for the benefit of a hypothetical member. Some commentators have **(p. 226)** not found this approach entirely illuminating but for the purposes of this appeal it is not necessary to discuss such cases any further. In this case, as in the *Stylo Shoes*case, it would have been perfectly rational to ask whether the vesting of voting control in Mr Tobias was in the interests of the company as a whole. …

21 Their Lordships therefore return to the present appeal. …

24 The Court of Appeal, reversing the judge, said (at paragraph 16) that where he went wrong in principle was 'when he attempted to step into the commercial arena'. Their Lordships take this to mean that the judge fell into the same error as Peterson J in *Dafen Tinplate Company Ltd v Llanelly Steel Company (1907) Ltd* **[4.25]**, namely that he took it upon himself to decide whether the amendment was for the benefit of the company. The Court of Appeal said that he should instead have applied the test laid down in *Shuttleworth's* case, namely, whether reasonable shareholders could have considered that the amendment was for the benefit of the company. The Court of Appeal considered that it would have been reasonable for shareholders to have accepted in good faith the arguments put forward by Mr Tobias as to why the amendment would be in the interests of the company. The only shareholder who gave evidence at the trial was Mr de Vos, who said that he had thought the amendments were in the best interests of the company as a whole. It was not necessary for Mr Tobias and the company to prove to the judge that the arguments were justified by the facts.

25 Their Lordships consider that this reasoning is correct. Mr Todd QC, who appeared for Citco, said that in a case in which one shareholder gained a personal advantage by the amendment, as Mr Tobias did in this case, it was necessary to show that even without his votes, the amendment would have been passed. In*Rights & Issues Investment Trust Ltd v Stylo Shoes Ltd* **[4.28]**, Pennycuick J laid some stress upon the fact that the resolution had been passed at a separate meeting of ordinary shareholders at which the holders of management shares did not vote. In this case there was, prior to the amendment, only one class of shares, but Mr Todd said that it was necessary to show that the resolution would have passed even without the votes controlled by Mr Tobias.

26 Their Lordships do not think that the *Stylo Shoes* case decided that in a case like this, shareholders who particularly stand to gain from the amendment should not vote. As Evershed MR said in *Greenhalgh v Arderne Cinemas Ltd* **[4.27]**, 291:

> 'It is … not necessary to require that persons voting for a special resolution should, so to speak, dissociate themselves altogether from their own prospects …'

27 If Mr Tobias bona fide considered that the amendment was in the interests of the company as a whole, and there has been no attack on his bona fides, their Lordships do not see why he should not vote. This is only one aspect of the general principle that shareholders are free to exercise their votes in their own interests. As Lord Davey said in *Burland v Earle*,[42] 94:

> 'Unless otherwise provided by the regulations of the company, a shareholder is not debarred from voting or using his voting power to carry a resolution by the circumstance of his having a particular interest in the subject-matter of the vote.'

28 In any case, it appears to their Lordships that even the test proposed by Mr Todd was satisfied. The only evidence as to the number of shares controlled by Mr Tobias was that of Mr de Vos, who said that it amounted to 28% of the issued share capital. He was cross-examined on this point, with counsel for Citco seeking to establish that Mr Tobias actually controlled very few shares, but stuck to 28%. He did also say that Mr Tobias was indirectly able to exercise the votes of 51% of the share capital, but this was consistent with the additional votes being simply those of supporters who had decided to entrust Mr Tobias with their proxies. Of the 28%, Mr Tobias did not vote the 62,439 shares registered in his own name. If he had not voted the 460,245 shares registered in the names of his **(p. 227)** wife and Piccadilly Properties Ltd, which made up the rest of the 28%, the votes cast in favour of the resolution would have been 665,420 out of a total of 848,420. This would still have been 78%.

29 Their Lordships will therefore humbly advise Her Majesty that the appeal should be dismissed with costs.

➢ Notes

1. The CLR took the view that the principle that a decision to change a company's articles must be taken bona fide for the benefit of the company as a whole was well established and should be retained. This was also the view adopted in *Citco* **[4.24]**.

2. It is rather curious that in both *Allen* **[4.22]** and *Sidebottom* **[4.23]** there are references to the good faith of the *directors*, when it is plain from the rest of the judgments that it is the bona fides of the majority members who pass the special resolution that is crucial. Of course, it would be easy to imagine a situation where the directors have an improper motive in introducing the proposal for change, and simply carry the opinion of the majority along with them. This may be what is being alluded to in the two cases. In fact, the directors in *Sidebottom*'s case held over half of the company's issued shares, and the majority in favour of the resolution was overwhelming.

➢ Question

Lord Hoffmann, at paragraph 18 of the *Citco* judgment, **[4.24]**, took the view that 'some other test' is needed where the proposed alteration concerns the 'rights of shareholders in matters in which the company as a corporate entity has no interest', since there it would be inappropriate 'to ask whether the shareholders had considered the alteration to be in the interests of the company as a whole'. What tests might meet this need? Where the company *has* an interest, the court accepts a*subjective* 'bona fide for the benefit of the company as a whole' test (subject to being persuaded of the bona fides). Where the company has *no* interest, and where there must inevitably be winners and losers as between different groups of shareholders, must the test necessarily be *objective* if the court is not simply to cede all power to the majority voter? See the next case cited.