law, are incapable of being ratified for some other reason. If Mr Sisley were right, the effect of section 239 would be to restrict the types of circumstance in which ratification is not possible because of wrongdoer control to those in which the connected person requirements of **(p. 660)** section 239(3) and (4) are satisfied. He did not suggest any policy reason why that might have been the Parliamentary intention and the passages from *Gore-Browne on Companies*… and *Palmer's Company Law*… suggest that it was not. In summary, I agree with the editors of *Palmer* that the connected person provisions in section 239(3) and (4) impose additional requirements for effective ratification which draw on existing equitable rules but which impose more stringent demands (*Palmer's Company Law* (25th edn) at paragraph 8.3412).

45 It follows that I consider that the words of Sir Richard Baggalay, delivering the advice of the Privy Council in *North-West Transportation Company v. Beatty* **[4.33]**, 594, describing the circumstances in which a company cannot ratify breaches of duty by its directors, remain good law:

> '… provided such affirmance or adoption is not brought about by unfair or improper means, and is not illegal or fraudulent or oppressive towards those shareholders who oppose it.'

It follows that, where the question of ratification arises in the context of an application to continue a derivative claim, the question which the court must still ask itself is whether the ratification has the effect that the claimant is being improperly prevented from bringing the claim on behalf of the company (c.f. Knox J in *Smith v. Croft (No 2)* **[13.17]**, 185B). That may still be the case where the new connected person provisions are not satisfied, but there is still actual wrongdoer control pursuant to which there has been a diversion of assets to persons associated with the wrongdoer, albeit not connected in the sense for which provision is made by section 239(4).

46 Mr Matthias submitted that the acts complained of are incapable of ratification because their effect was to oppress the minority by driving down the value of Franbar's minority interest, in any event when seen against the background of the options contained in the Shareholders' Agreement. This might be correct in relation to a number of the breaches alleged against Mr Patel and Dr du Plessis, but it cannot sensibly be said that every breach of duty pleaded in the derivative claim is incapable of ratification merely because it caused sufficient loss to Medicentres to have an effect on the value of Franbar's shares. In my judgment, that would be to give a meaning to the concept of minority oppression which is not justified by the authorities.

47 I do, however, accept that some of the complaints made by Franbar may well be incapable of ratification. It seems to me that, if Franbar were to establish its claim that some part of the business of Medicentres, or some business opportunity which properly belonged to it, had been diverted to Casualty Plus at the suit of Mr Patel or Dr du Plessis, that may well amount to a breach of duty incapable of ratification on the votes of Casualty Plus, more particularly if it was done with the intention of driving down Medicentres' earnings and reducing the amount payable to Franbar on exercise of the option. Despite Mr Sisley's comprehensive submissions on the improbability of any such breach being established, I am unable to say at this stage that he is right. In my judgment it is possible that Franbar will establish at trial that, in all the circumstances of the case, some of the breaches alleged will prove to be incapable of ratification. In this, as in many cases, it is only possible to say at this stage that, while it is likely that an attempt will be made to ratify all of the breaches, it is no more than a possibility that ratification of all of the breaches will prove to be effective.

48 The fourth relevant matter of which I am required to take particular account is whether Medicentres has decided not to pursue the claim. Mr Matthias submitted that Medicentres has made no such decision and Mr Sisley did not contend that it had. I am able to infer, however, that if it were to engage in a formal consideration of whether or not to pursue the claim, Medicentres would decide not to do so. In a case such as the present, this seems to me to add little to the issue of ratification which I have already considered.

➢ Question

The previous case suggests that not only are the wrongdoers and connected persons barred from the ratification vote (CA 2006 s 239), but that certain wrongs are simply 'unratifiable', even by an untainted majority. Which wrongs are 'unratifiable'? Are such wrongs unratifiable because of the nature of the wrong or because of the nature of the ratification decision? **(p. 661)** *Should* any wrongs be unratifiable? Where a wrong *is* ratifiable, how does effective ratification take place? See the following Notes.

➢ Notes

1. In *Cook v Deeks* **[6.15]**, at 564, Lord Buckmaster took the view that if:

> the contract in question was entered into under such circumstances that the directors could not retain the benefit of it for themselves, then it belonged in equity to the company and ought to have been dealt with as an asset of the company. Even supposing it be not *ultra vires* of a company to make a present to its directors, it appears quite certain that directors holding a majority of votes would not be permitted to make a present to themselves. This would be to allow a majority to oppress the minority. To such circumstances the cases of *North-West Transportation v Beatty* **[4.33]** and *Burland v Earle* [1902] AC 83, PC, have no application.

2. In *Daniels v Daniels* [1978] Ch 406, three minority shareholders brought an action against Mr and Mrs Daniels, the two directors and majority shareholders of the company, alleging *negligence* (rather than breach of the conflicts rules), in that they had negligently caused the company to sell land to Mrs Daniels at a fraction of its true value. In preliminary proceedings, Templeman J held that the plaintiffs had standing to sue, notwithstanding *Foss v Harbottle*. He said:

> The authorities which deal with simple fraud on the one hand and gross negligence on the other do not cover the situation which arises where, without fraud, the directors and majority shareholders are guilty of a breach of duty which they owe to the company, and that breach of duty not only harms the company but benefits the directors. In that case it seems to me that different considerations apply. If minority shareholders can sue if there is fraud, I see no reason why they cannot sue where the action of the majority and the directors, though without fraud, confers some benefit on those directors and majority shareholders themselves. … To put up with foolish directors is one thing; to put up with directors who are so foolish that they make a profit of £115,000 odd at the expense of the company is something entirely different. The principle which may be gleaned from *Alexander v Automatic Telephone Co*[26] (directors benefiting themselves), from *Cook v Deeks* **[7.22]**(directors diverting business in their own favour) and from dicta in *Pavlides v Jensen*[27] (directors appropriating assets of the company) is that a minority shareholder who has no other remedy may sue where directors use their powers, intentionally or unintentionally, fraudulently or negligently, in a manner which benefits themselves at the expense of the company.

3. *Daniels v Daniels* is always contrasted with *Pavlides v Jensen* [1956] Ch 565 where a minority shareholder unsuccessfully attempted to bring an action against the directors alleging negligence in the sale of an asbestos mine to an associated company at a gross undervalue. The directors objected that the shareholder had no right to sue, and the court agreed, there being no evidence of fraud or personal benefit.[28] Is the case legitimately distinguishable on this basis?

4. Is it true that *Cook v Deeks* **[7.22]** and *Daniels v Daniels*, in the previous Notes, represent a category of 'unratifiable wrongs'? If so, *should* this be allowed, or should it be left to CA 2006 s 239 to deal straightforwardly

with these cases, and cases such as *Regal (Hastings) Ltd v Gulliver* **[7.23]** (corporate opportunity) and *North-West Transportation v Beatty* **[4.33]** (self-dealing)? (While noting s 239(7)!)

(p. 662) ***The court must consider whether the member has alternative personal claims which could be pursued in his own right rather than on behalf of the company: s 263(3)(f).***

[13.13] Franbar Holdings Ltd v Patel [2008] EWHC 1534 (Chancery Division)

For the facts, see **[13.08]**. Also see **[13.12]**.

MR WILLIAM TROWER QC:

50… What is required is for the act or omission of which complaint is made to give rise to a cause of action available to the member in its own right. Doubtless such a cause of action will sometimes be a claim seeking relief against the same director defendants, but I do not read the subsection as being limited to such claims. In my view, the only limitation is that the cause of action should arise out of the same act or omission; where that act or omission gives rise to both a claim for unfair prejudice against a member and a claim for breach of duty against a director, s 263(3)(f) is engaged. The adequacy of the remedy available to the member in his own right is, however, a matter which will go into the balance when assessing the weight of this consideration on the facts of the case. Even if this is wrong as a matter of strict construction of the subsection, I consider that it is relevant in the present case for the court to see whether the acts or omissions in respect of which the derivative claim is brought give rise to a cause of action that the member can bring against another person. That is a consideration of some significance where that other person is the majority shareholder with close connections to the directors concerned, and where the buy-out offer which has already been made is made on behalf of all of the Defendants.

51 I can well understand why Mr Matthias accepted the extent of the overlap between the s 994 petition and the derivative claim and I think that he was right to do so. In my view most, if not all, of the allegations of breach of duty to Medicentres (and certainly all those which are even arguably incapable of ratification) are likely to be relevant to Franbar's complaint of unfair prejudice. Furthermore, the losses which Medicentres might have sustained as a result of the breaches of duty pleaded in the derivative claim are relevant to the fair value of Franbar's shares and to the question of what factual assumptions should be made on the valuation to ensure that Franbar is put into the position that it would have been in but for the unfair prejudice which it will (on this hypothesis) have established. I can see no reason why Franbar should not be granted such relief on the unfair prejudice petition as may be necessary to ensure that the interest which it seeks to realise is valued on a basis which takes full account of the value of the complaints it wishes to pursue on behalf of Medicentres in the derivative claim.

52 In the end, it was clear that Franbar's real concern was that Casualty Plus might not be in a position to pay a fair value for Franbar's shares in Medicentres (having regard to the value of Medicentres' claims against Mr Patel and Dr du Plessis), while a judgment against Mr Patel and Dr du Plessis is one which is more likely to be satisfied, or in any event gives Franbar an extra string to its bow. There is some foundation for this concern because it seems possible that Casualty Plus will have to raise additional capital to fund its purchase of Franbar's shares and may have difficulty in doing so, although I give this consideration less weight in the light of the fact that the open offer to purchase is one to which each of the Defendants is a party.

53 Franbar also submits that continuation and consolidation will be a cost effective and proportionate way of resolving all claims between the parties. It is said that this is a more efficient way of dealing with the dispute than leaving over the possibility that a derivative claim might have to be pursued in due course, once unfair prejudice has been established. I cannot rule out the possibility that a derivative claim may need to be pursued at a later stage, but I am bound to say that it seems to me most unlikely that this will be necessary. In this particular case, the availability (and indeed use) of both the s 994 petition and the shareholders' action weigh in the balance against the grant of permission to continue the derivative action. Any possible future difficulty in enforcing a buy-out order against Casualty Plus is not, anyway at this stage

of the proceedings, a sufficiently powerful **(p. 663)** basis for taking another view. I also take into account the fact that continuing with a further set of proceedings at this stage might well give rise to unnecessary further complexity in the future, even if those proceedings were to be consolidated with the s 994 petition and even though Franbar has now abandoned (in any event for the present) its application for an indemnity from Medicentres in respect of its costs.

[13.14] Kiani v Cooper [2010] EWHC 577 (Chancery Division)

For the facts, see **[13.11]**.

PROUDMAN J:

38 Another factor prescribed by s 263(3) is the availability to Mrs Kiani of an alternative remedy in respect of the alleged breaches of duty. Mr Irvin submits that one proper remedy would be a personal action under the shareholders' agreement. However, it seems to me that such an action could meet real difficulties in that the loss claimed could be viewed as loss reflective of the company's loss, irrecoverable under the principle enunciated in *Johnson v Gore Wood* **[13.22]**.

39 Mr Irvin's principal submission is however that Mrs Kiani's proper remedy is an unfair prejudice petition under CA 2006 s 994. Under s 994 the court has a very wide discretion as to the relief it may grant, including, by s 996(2)(c), authorising civil proceedings in the name of and on behalf of the company.

40 There is a lot to be said for this procedure in a case of a two-person company where the real dispute is between those two persons alone. However, the jurisdiction to make an order under s 996(2)(c) can only be exercised if the court is first satisfied that the unfair prejudice petition is well-founded. Mrs Kiani would not therefore have standing on behalf of the company to restrain a winding up petition. It may well be the case that the court would have jurisdiction on her application to restrain a winding up petition pending the outcome of s 994 proceedings. I have not been addressed on that issue. Moreover, yesterday Mr Cooper and DPM, through Mr Irvin, said for the first time that they were willing to offer an undertaking not to present creditors petitions pending s 994 proceedings.

41 Taking all those factors into consideration, it seems to me that Mrs Kiani's position is this. She says that she and the company have been deprived of the opportunity to pursue the development venture. She does not want the company to be wound up on the petition of Mr Cooper, at whose door she places responsibility for the deadlock which has occurred. She wants her opportunity to be preserved. She wishes to pursue Mr Cooper on behalf of the company in a derivative action. It seems to me that the fact that she could in a more roundabout way achieve the relief she seeks does not mean that she ought not to be granted permission in the present case. It is merely one of the factors that I have to take into account.

[13.15] Stainer v Lee [2010] EWHC 1539 (Chancery Division)

Also see **[13.05]**.

A minority shareholder (S) in company C was permitted to continue a derivative claim against two of C's directors in respect of what appeared to be substantial interest-free loans made by C to company E which was owned by one of those directors. E had been established as a special purpose vehicle (SPV) for the acquisition of shares in C. By 2002, it had acquired a 65% shareholding in C with the aid of a bank loan exceeding £4 million. This debt was repaid out of interest-free loan funds from C to E. The failure to obtain interest for C over a period of almost nine years on lending to E that rose from £4.6 million to £8.1 million constituted very strong grounds for a claim that the directors were in breach of their fiduciary duties. The judge held that it was therefore appropriate to grant S permission to continue the derivative claim until the conclusion of disclosure.

(p. 664) ROTH J:

50 The Respondents also contend that this is a case that the Applicant could pursue by an 'unfair prejudice' petition under section 994, and thus in his own right, which is a relevant consideration under section 263(3)(f). As Lewison J observed in *Iesini* **[13.10]** the availability of the alternative remedy is included under sub-section 263(3) not 263(2) and is accordingly a discretionary consideration not an absolute bar.

51 In many cases, an allegation of breach by directors of their fiduciary duties could found an unfair prejudice petition as well as a derivative action. But that should not disguise the fundamentally different nature of the two forms of proceedings. As Millett J explained in *Re Charnley Davies Ltd (No 2)* [1990] BCLC 760 at 784:

> 'The very same facts may well found either a derivative action or a s [994] petition. But that should not disguise the fact that the nature of the complaint and the appropriate relief is different in the two cases. Had the petitioners' true complaint been of the unlawfulness of the respondent's conduct, so that it would be met by an order for restitution, then a derivative action would have been appropriate and a s [994] petition would not. But that was not the true nature of the petitioners' complaint. They did not rely on the unlawfulness of the respondent's conduct to found their cause of action; and they would not have been content with an order that the respondent make restitution to the company. They relied on the respondent's unlawful conduct as evidence of the manner in which he had conducted the company's affairs for his own benefit and in disregard of their interests as minority shareholders; and they wanted to be bought out. They wanted relief from mismanagement, not a remedy for misconduct.'

52 In the present action, the Applicant is not seeking to be bought out. He commenced these proceedings, with the support of 35 other minority shareholders, seeking financial remedies for misconduct against the two directors personally, and now an order for restitution from Eldington. Such orders could not be made on an unfair prejudice petition, albeit that the court could by way of remedy authorise the bringing of proceedings in the name of the company by the petitioner: section 996(2)(c). But that would then give rise to a subsequent and further set of proceedings. I consider that given what is at the heart of the present case, a derivative action is entirely appropriate and therefore the theoretical availability to the Applicant of proceedings by way of an unfair prejudice petition is not a reason to refuse permission.

[13.16] Kleanthous v Paphitis [2011] EWHC 2287 (Chancery Division)

Also see **[13.06]**.

Mr Kleanthous was a shareholder in Ryman Group Limited (RGL), the three subsidiaries of which were engaged in the fields of stationery, lingerie and mobile telephone businesses respectively. Mr Kleanthous complained that the other directors had breached their fiduciary duties owed to RGL, by virtue of their decision to enable one of their number, Mr Paphitis, to acquire La Senza, a listed company also engaged in the lingerie business. Mr Kleanthous argued that Mr Paphitis and his company had been enabled to develop this opportunity as well as to use assets of RGL for their own benefit. It was further contended that the defendants had made very substantial profits which resulted in enormous loss to RGL. Newey J refused permission to continue the claim on the basis that the claim was not of such strength and size as could make it appropriate for permission to be granted when (i) that course was strongly opposed, on a reasoned basis, by the Ryman Companies' independent committees as well as by Mr Childs (who was accepted by the court as being disinterested in the alleged conflicts); (ii) that other means of redress were available under CA 2006 s 994; and (iii) much of the money recovered by the company from the director defendants could be expected to be returned to them by way of distribution.

(p. 665) NEWEY J:

78 In *Franbar Holdings Ltd v Patel* **[13.13]**, Mr William Trower QC, sitting as a Deputy High Court Judge,

gave considerable weight to the fact that the Claimant should be able to achieve all that it could properly want through a s 994 petition and shareholders' action which were already on foot (see paragraphs 53 and 54). In*Iesini v Westrip Holdings Ltd* **[13.10]**, Lewison J said (in paragraph 126) that the availability of an alternative remedy under s 994 was one of the factors which would have led him to the conclusion that, had he not adjourned the matter, it would not have been appropriate to allow a derivative claim to proceed.

79 In contrast, the availability of an alternative remedy under s 994 did not appear to the Inner House to be a compelling consideration on the facts of *Wishart v Castlecroft Securities Ltd* [2009] CSIH 65, where Lord Reed commented (in paragraph 46) that such proceedings would 'constitute, at best, an indirect means of achieving what could be achieved directly by derivative proceedings'. Similarly, in *Stainer v Lee* **[13.15]** Roth J considered a derivative action 'entirely appropriate' and 'the theoretical availability to the applicant of proceedings by way of an unfair prejudice petition … not a reason to refuse permission'; the applicant was 'not seeking to be bought out' (paragraph 52).

80 In the present case, likewise, it was submitted on Mr Kleanthous' behalf that he was not seeking a buy-out of his shares. However, the evidence indicates that Mr Kleanthous is interested in being bought out. [The judge referred to various witness statements, and to proposed action under s 994.]… One is left with the suspicion that Mr Kleanthous has chosen to pursue derivative proceedings alone in the hope that he will be able to obtain a costs indemnity (with the result that the other shareholders in RGL would be likely to bear the bulk of the costs even if the claims against them failed).

81 In all the circumstances, I agree with Mr Todd that the availability of an alternative remedy in the form of an unfair prejudice petition is a powerful reason to refuse permission for the derivative claim to proceed in this case.

➢ Note

Where practical considerations demand, such as the urgent need for a summary judgment for the recovery of money misappropriated, and to stop more money from being taken, the claimant may be allowed to change his mind and bring a derivative action *in addition* to a s 994 petition: *Phillips v Fryer* [2012] EWHC 1611 (Ch).

➢ Question

Compare the previous cases. Are the courts' approaches consistent? What features render the alternative remedy more than a mere 'theoretical availability' (per Roth J in *Stainer v Lee* **[13.15]**)?

In exercising its discretion, the court shall have particular regard to the views of the members of the company who have no direct or indirect personal interests in the matter: s 263(4).

[13.17] Smith v Croft (No 2) [1988] Ch 114 (Chancery Division)

This case pre-dates the CA 2006 changes, but reflects their import. The claimants were minority shareholders claiming (inter alia) to recover, on behalf of their company, sums which had been paid away in transactions which were both *ultra vires* and in breach of the statutory prohibition on financial assistance ('Financial assistance by a company for the acquisition of its own shares', pp 524ff). With their supporters, the plaintiffs had 14% of the voting rights in the company and the defendants 63%; and there were other shareholders commanding 21% of the votes who did not wish the litigation to proceed. Knox J held that: (i) a prima facie case **(p. 666)** of *ultra vires* and illegality had been made out, for which the company was entitled to relief; (ii) the plaintiffs accordingly had standing to bring a derivative action; but that (iii) the plaintiffs nevertheless had no right to sue if a majority of the shareholders who were independent of the defendants did not want the action to continue.

KNOX J: Another way of putting the question is to ask whether if a minority has been the victim of a fraud entitling the company in which they are shareholders to financial redress, the majority within that minority can prevent the minority within that minority from prosecuting the action for redress. The usual reason in practice for wanting to abandon such an action is that there is far more to lose financially by prosecuting the right to redress than by abandoning or not pursuing it, and that view will be reinforced in the minds of those who wish to abandon the claim if their opinion is that it is a bad claim anyway. …

Mr Potts [counsel] submitted that no reported authority held that in a case falling within the fraud on a minority exception to the rule in *Foss v Harbottle* the court should go beyond seeing whether the wrongdoers are in control and count heads to see what the other shareholders, ie those other than the plaintiff and the wrongdoers, think should be done. I accept that in many reported cases the court has not gone on to the second stage.

… Ultimately the question which has to be answered in order to determine whether the rule in *Foss v Harbottle* applies to prevent a minority shareholder seeking relief as plaintiff for the benefit of the company is 'Is the plaintiff being improperly prevented from bringing these proceedings on behalf of the company?' If it is an expression of the corporate will of the company by an appropriate independent organ that is preventing the plaintiff from prosecuting the action he is not improperly but properly prevented and so the answer to the question is 'No'. The appropriate independent organ will vary according to the constitution of the company concerned and the identity of the defendants who will in most cases be disqualified from participating by voting in expressing the corporate will. [His Lordship then held that a majority of shareholders, excluding the defendants but including the Wren Trust (which he ruled was 'independent'[29]) were opposed to continuing the action, and ordered that it should be struck out.]

Costs.

[13.18] Kiani v Cooper [2010] EWHC 577 (Chancery Division)

For the facts and another part of the judgment, see **[13.11]**. Also see **[13.14]**.

PROUDMAN J:

47 That brings me to the second issue, which is the discrete one whether Mrs Kiani should be indemnified from the company's assets in respect of her costs. Mr Dougherty pressed me to make such an order. He said this is the usual order. He submitted that the claim is properly brought on behalf of the company in accordance with the statutory framework. The company is the loser as a result of the acts and defaults of the director and there is no justification for departure from the usual course. He prayed in aid the well-known comments of Lord Denning, Master of the Rolls, in *Wallersteiner v Moir (No 2)*.[30]

(p. 667) 48 However, it seems to me that in a case of this kind, where the dispute is one between the two directors and shareholders, the court ought to take a realistic view. There are no significant unsecured creditors of which Mrs Kiani is aware whose interests come into the equation. There is some analogy with the trustee beneficiary who brings a *Beddoe* summons for directions to sue his fellow trustee beneficiary and asks for his costs of doing so out of the fund. In such circumstances the court is likely to refuse to force the defendant to fund proceedings against him. The claimant must take the risk as to costs.

49 On that basis I am prepared to make an order that Mrs Kiani's costs should be borne by the company, but I am not prepared to grant her an indemnity in respect of any adverse costs order, that is to say, any order that Mr Cooper or DPM should be entitled to costs. It seems to me that she should be required to assume part of the risk of the litigation. However, that part of the order will be subject to review after disclosure.

Personal claims by members

All these pitfalls associated with derivative claims can be avoided if members can pursue *personal* remedies for any wrongs done to them. Much of the relevant substantive law has been addressed in earlier chapters. The one omission is an enormously significant one. Members have a statutory right to complain to court that the company's affairs are being conducted in a manner that is unfairly prejudicial to the member's interests (CA 2006 s 994). This provision is commonly known as the '*unfair prejudice*' section. The court has wide powers to make orders as it sees fit if a claim of unfair prejudice is made out (s 996). The relevant rules are discussed in detail at 'Unfairly prejudicial conduct of the company's affairs', pp 681ff. In addition, members have the right to petition for the company to be wound up on the 'just and equitable' ground. These rules are discussed in detail at 'Compulsory winding up on the "just and equitable" ground', pp 795ff. First, however, it is necessary to consider some of the more general issues that are relevant to pursuit of personal claims by members.

The sources of members' personal rights

Members' claims for a personal remedy are generally based on wrongs committed in relation to:

(i) The contractual rights derived from the *company's constitution* (CA 2006 s 33):[31] see 'Members' personal rights', pp 250ff. Recall the difficult learning on the nature of the statutory contract, including the distinction between 'insider' and 'outsider' rights. In addition, these claims are subject to the 'internal irregularity principle' imposed by *Foss v Harbottle*: see *Macdougall v Gardiner* **[13.20]** and *Pender v Lushington* **[13.19]**. These rights are relevant in the pursuit of claims concerning amendments to the constitution, variations of class rights, capital reductions, etc, at least to the extent that the shareholder is not simply relying on specific statutory rights given to dissenting minorities to complain.
(ii) The contractual rights derived from outside contracts, especially *shareholders' agreements*:[32] see 'Shareholders' agreements', pp 244ff. See especially *Southern(p. 668) Foundries (1926) Ltd v Shirlaw* **[6.04]**, *Read v Astoria Garage (Streatham) Ltd* **[6.05]** and *Russell v Northern Bank Ltd* **[4.34]**.
(iii) The *duties owed by directors* to members individually, in those rare cases where this can be asserted successfully: see 'Directors' duties are rarely owed to individuals within or associated with the company', pp 321ff. See especially *Percival v Wright* **[7.05]**; *Peskin v Anderson* [2001] BCLC 874, CA; *Coleman v Myers*[1977] 2 NZLR 225 and also see 'Offers to the public to purchase shares and remedies for misleading offers', pp 499ff.
(iv) The entitlements inherent in the 'unfair prejudice' section (CA 2006 s 994): see 'Unfairly prejudicial conduct of the company's affairs', pp 681ff. This section provides a procedural mechanism for a member to raise a wide variety of complaints, including those noted in points (i)–(iii), although the court cannot give a remedy unless the 'unfair prejudice' basis is established. But this section also permits shareholders to complain of, and obtain legal remedies for, acts and omissions that do not of themselves constitute legal wrongs.
(v) The entitlements inherent in the 'just and equitable' winding-up provisions (IA 1986 s 122(1)(g)): see 'Compulsory winding up on the "just and equitable" ground', pp 795ff.

The procedural form of members' personal claims

Two types of proceedings may be brought by shareholders to enforce personal rights. These need to be distinguished from the derivative claim discussed earlier (see 'The statutory derivative action: CA 2006 ss 260ff', p 642):

(i) A member may sue alone to enforce some personal or individual right: for instance, in *Pender v Lushington* **[13.19]** the right to have a vote recorded or a proxy recognised. *Rayfield v Hands* **[4.38]** shows that the company is not a necessary party to such proceedings—unless, of course, it is claimed that the company is a party to the wrongdoing.
(ii) A member may sue alone, or with others, but in a *representative* capacity, claiming that a right has been infringed which, although affecting him as an individual member, also affects in a similar way either all or a number of the other members. Cases where a member has succeeded in a claim to have the directors observe the requirements of the Act or the constitution of the company itself are examples of this kind of

action. This is a *representative action*.[33]

(p. 669) Establishing the member's personal right: personal and corporate claims can coexist

Sometimes it is very clear that the member has a personal right. But not all wrongs that a member complains of will be exclusively one thing or the other: an unconstitutional act by those in control may violate *both* shareholder's individual membership rights *and* those of the company, as has been recognised on many occasions: see, eg *Pulbrook v Richmond Consolidated Mining Co* **[6.01]** and *Pender v Lushington* **[13.19]**.

It ought to be possible in such cases for an action to be brought in the name of either the member or the company (for different remedies), but unfortunately the courts have not always appreciated this. We find them giving an individual complainant short shrift and showing him the door of the court on the basis of a somewhat peremptory ruling that the wrong person has been named as plaintiff.[34] For example, see *Lee v Chou Wen Hsien* (Question 3 following *Pender v Lushington* **[13.19]**, p 671); and contrast the views of Hoffmann J in *Re a Company* (Note 2 in Further notes following *Pender v Lushington* **[13.19]**, p 671) with those expressed in *Bamford v Bamford* [1970] Ch 212 (see Note 1 in Further notes following *Pender v Lushington* **[13.19]**, p 671). This sometimes seems to provide further proof of a *de facto* policy to discourage minority members from engaging in litigation. Added to this, there is the modern debate on '*reflective loss*', which aims to ensure that if both forms of action are possible, there is no chance of double recovery for the same loss (see 'The "no reflective loss" principle', pp 673ff).

An individual member whose personal rights have been infringed may pursue a personal claim even when the conduct complained of also constitutes a wrong to the company itself.

[13.19] Pender v Lushington (1877) 6 Ch D 70 (Chancery Division)

Pender had split his shareholding among nominees in order to defeat a provision in the articles that fixed the maximum number of votes to which any one shareholder was entitled. The chairman refused to accept the nominees' votes and accordingly declared lost a resolution proposed by Pender, which would otherwise have been carried. The Master of the Rolls granted Pender (who brought a representative action on behalf of himself and the other shareholders, and also an action in the name of the company) an injunction restraining the directors from acting on the basis that the nominees' votes had been bad. He also held that Pender had a right to sue in the company's name, at least until a general meeting resolved otherwise,[35] and a further right to sue in his own name.

> JESSEL MR: But there is another ground [other than the claim in the company's name] on which the action may be maintained. This is an action by Mr Pender for himself. He is a member of the company, and whether he votes with the majority or the minority he is entitled to have his vote recorded—an individual right in respect of which he has a right to sue. That has nothing to do with the question like that raised in *Foss v Harbottle* and that line of cases. He has a right to say, 'Whether I vote in the majority or minority, you shall record my vote, as that is a right of property belonging to my interest in this company, and if you refuse to record my vote I will institute legal proceedings against you to compel you'. What is the answer to such an action? It seems to me it can be maintained as a matter of substance, and that there is no technical difficulty in maintaining it …

(p. 670) ➢ Notes

1. The real problem in these cases is to determine whether a member *does* have a personal right, and one that can be pursued despite the 'irregularity principle' in *Foss v Harbottle*: see *Macdougall v Gardiner* **[13.20]**, which is difficult to reconcile with *Pender v Lushington*.

2. Personal rights do arise under some basic constitutional provisions, such as the right to vote or to exercise a pre-emptive power over a retiring member's share, and*Edwards v Halliwell* [1950] 2 All ER 1064, CA, illustrates the right in operation in a trade union context, protecting a member against having his dues raised

without proper procedure and from unjustifiable expulsion. But all these 'constitutional' rights have an element of property linked with them, so it is easier to understand the readiness of the courts to come to the aid of a victimised member.

3. Where the complaint is about a mere matter of procedure, the courts seem much less willing to recognise a 'right to have the company observe the terms of its own constitution' which an individual member might invoke to claim standing to sue. One difficulty about such a supposed right is that it is balanced by an obligation to abide by majority decisions (see *Smith v Croft (No 2)* **[13.17]**). Another is that there are some constitutional irregularities which members may waive by a majority vote, or even, on the reasoning of *MacDougall v Gardiner* **[13.20]**, simply acquiesce in. Certainly, *obiter dicta* in cases such as *Re HR Harmer Ltd* [1959] 1 WLR 62, CA (see Note following *Scottish Co-operative Wholesale Society Ltd v Meyer* **[13.24]**, p 685), to the effect that members have a right to have their company conduct its affairs in accordance with its articles cannot be understood to apply without some such qualification.

4. Another difficulty concerns rights purportedly conferred on members by the company's articles, but not in their character as members. Cases like *Eley v Positive Life Assurance Co* **[4.36]** are accepted as laying down a rule that 'outsider rights' are not enforceable on a contractual basis by the member against the company. Nor can this rule be avoided simply by bringing an action as a 'member' to compel the company to comply with its 'constitutional obligations' to recognise the right. But the distinction between 'insider' and 'outsider' rights is not always clear. In *Pulbrook v Richmond Consolidated Mining Co* **[6.01]**, a director who had been excluded from board meetings was held to have suffered an individual wrong, and held able to sue in his own name; also see *Quin and Axtens Ltd v Salmon* **[4.06]**.

5. Of course, if the member *waives* the personal right, then there can be no complaint later on, even if it becomes apparent that the waiver was unwise. For example, in*Euro Brokers Holdings Ltd v Monecor (London) Ltd* [2003] EWCA Civ 105, special decision-making procedures were set out in a shareholders' agreement specifically to protect the interests of certain members. All the members nevertheless took a decision, unanimously, without following the special procedures. The decision was held valid. The key point in this case, however, was that the decision attracted the support of all members at the time, and the court therefore held that it should not be subsequently reviewable on the basis of non-compliance with some specified procedure. In *Edwards v Halliwell* [1950] 2 All ER 1064, CA, situations, it is precisely the lack of agreement to waive the special procedural requirements on the part of those protected by such requirements which gives rise to the arguments about personal rights and exceptions to the rule in *Foss v Harbottle*.

➢ Questions

1. In *Pender v Lushington* **[13.19]**, if a general meeting had been called and had voted against continuing the action, what would have happened to Pender's personal and derivative claims?

2. In *Devlin v Slough Estates Ltd* [1983] BCLC 497 a member sought a declaration that the directors had acted in breach of duty. He alleged that they had prepared accounts which failed **(p. 671)** to conform with the requirements of the Companies Acts, and also that they had failed to distribute accounts properly prepared in accordance with the Acts to the members in advance of the annual general meeting as required by the company's articles. Dillon J held that Devlin did not have standing to bring either a derivative action on the company's behalf or an action in his own right complaining that his personal rights as a member had been infringed. How, if at all, can Dillon J's decision be reconciled with *Edwards v Halliwell, Pender v Lushington* and the previous Note?

3. In *Lee v Chou Wen Hsien* [1984] 1 WLR 1202, the plaintiff sued in his own name complaining that he had been improperly removed as a director by his fellow directors, who had purportedly acted under a power conferred by the articles. The Privy Council took the view that if a wrong had been done, it was done to the*company*, and that the rule in *Foss v Harbottle* precluded any action by the director in his own name. Do you agree?

➤ ***Further notes***

This area is difficult, and the cases are not easy to reconcile. Yet, if members are to pursue personal claims, then it is essential to know whether the wrong in question is one which has been done to the company or to the member personally, since in the latter circumstances the member, being the proper claimant, is able to sue, subject only to the 'internal management' and 'irregularity' principles (see 'The old common law rule in *Foss v Harbottle*', pp 639ff). The following examples further illustrate the courts' approach.

1. In *Bamford v Bamford* [1970] Ch 212 (for the facts and another part of the decision, see **[4.32]**), Russell LJ held that:

> The harm done by the assumed improperly motivated allotment is a harm done to the company, of which only the company can complain. It would be for the company by ordinary resolution to decide whether or not to proceed against the directors for compensation for misfeasance.

2. By contrast, in *Re a Company* [1987] BCLC 82, at 84, Hoffmann J said:

> Although the alleged breach of fiduciary duty by the board is in theory a breach of its duty to the company, the wrong to the company is not the substance of the complaint. The company is not particularly concerned with who its shareholders are. The true basis of the action is an alleged infringement of the petitioner's individual rights as a shareholder. The allotment is alleged to be an improper and unlawful exercise of the powers granted to the board by the articles of association, which constitute a contract between the company and its members. These are fiduciary powers, not to be exercised for an improper purpose, and it is generally speaking improper 'for the directors to use their fiduciary powers over the shares in the company purely for the purpose of destroying an existing majority, or creating a new majority which did not previously exist'. (See *Howard Smith Ltd v Ampol Petroleum Ltd* **[7.12]**.) An abuse of these powers is an infringement of a member's contractual rights under the articles.

3. Similarly, in *Residues Treatment and Trading Co Ltd v Southern Resources Ltd (No 4)* (1988) 14 ACLR 569, the Supreme Court of South Australia held that an action to challenge an allotment of shares on the ground that the directors had acted for an improper purpose came within the 'personal rights' exception to the rule in *Foss v Harbottle* **[13.01]** (as well as being a breach of duty to the company for which the company itself could have sued), since such an allotment brought about an impermissible dilution of the plaintiff member's voting rights. King CJ said, at 575:

> A member's voting rights and the rights of participation which they provide in the decision-making of the company are a fundamental attribute of membership and are rights which the member should be able to protect by legal action against improper diminution.

(p. 672) (He also expressed doubts whether *Bamford v Bamford*, Note 1, was correct in treating such an act on the part of the directors as ratifiable by the members, but it is suggested that *Bamford v Bamford* may be defended on this point.)

4. Finally, in *MacDougall v Gardiner* (1875) 10 Ch App 606, the member had an undoubted personal right under the articles, but the Court of Appeal nevertheless held that it had no jurisdiction to cure the improper denial of the member's right to call for a poll, since this was an irregularity which could be cured by the majority. James LJ drew attention to the good sense that lies behind the normal constitutional provisions which allow a meeting to be requisitioned, or conducted in a particular manner, only when a significant percentage of supporters can be mustered. (But contrast *Pender v Lushington* **[13.19]**.)